

# THE SCHOOLS AND LIBRARIES INTERNET ACCESS ACT

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HEARING  
BEFORE THE  
SUBCOMMITTEE ON TELECOMMUNICATIONS,  
TRADE, AND CONSUMER PROTECTION  
OF THE  
COMMITTEE ON COMMERCE  
HOUSE OF REPRESENTATIVES  
ONE HUNDRED SIXTH CONGRESS  
FIRST SESSION

ON

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(III)

## THE SCHOOLS AND LIBRARIES INTERNET ACCESS ACT

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THURSDAY, SEPTEMBER 30, 1999

HOUSE OF REPRESENTATIVES,  
COMMITTEE ON COMMERCE,  
SUBCOMMITTEE ON TELECOMMUNICATIONS,  
TRADE, AND CONSUMER PROTECTION,  
*Washington, DC.*

The subcommittee met, pursuant to notice, at 10:17 a.m., in room 2322, Rayburn House Office Building, Hon. W.J. "Billy" Tauzin (chairman) presiding.

Members present: Representatives Tauzin, Cox, Rogan, Shimkus, Wilson, Ehrlich, Markey, Rush, Wynn, and Sawyer.

Staff present: Linda Bloss-Baum, majority counsel; Justin Lilley, majority counsel; Mike O'Reilly, professional staff; Cliff Riccio, legislative clerk; and Andy Levin, minority counsel.

Mr. TAUZIN. Good morning, my apologies. Among my many duties around here is the deanship of the Louisiana delegation. We had one of those rare delegation meetings this morning.

When Congress passed the Telecommunications Act in 1996, they included the idea of a program for the discount of advanced telecommunications services for organizations that would most need assistance acquiring the technology of the Internet; namely, schools, libraries, and rural health care centers. The FCC broadly interpreted the statute to require subsidies not only for basic telephone service for schools but also for Internet access, content based information services, and equipment for internal connections.

They have even created now a new bureaucracy to take over the administration of the program, the Schools and Libraries Division of the Universal Service Administration Company. Furthermore, the FCC took it upon themselves to create a \$2.5 billion fund to be developed by excise taxes on every consumer's phone bill. This type of what I consider to be illegal taxation was certainly not the intention of Congress.

After some urging from Chairman Bliley and myself last May, the FCC scaled back their original \$2.5 billion program to \$1.3 billion. The fact is, I believe that neither the FCC nor the FCC-created USAC has the authority to levy taxes. Only Congress, unfortunately, can do that. Unfortunately, we have to take on that duty once in a while, which is why I introduced the Schools and Libraries Internet Access Act, H.R. 1746.

With this bill, we reassert control over Congress' original idea that the Schools and Libraries Internet Access Act would cut taxes, not increase them. The bill cuts the existing regressive 3 percent

telephone excise tax, passed in 1913, by fully two-thirds over 5 years. That tax was passed in 1913 to fund World War I, which if history serves me right I think is over, but the tax is not.

After the fifth year under our bill, when all the schools have been connected to the information superhighway, the bill completely repeals the rest of the tax. The bill removes the program from the FCC and puts it into the hands of State educational officials and the National Telecommunications Information Administration of the Department of Commerce.

The bill would meet our goal of bringing advanced telecommunications services and the Internet to our neediest schools and libraries and will eliminate the need for improper new taxes imposed by the FCC, which many have, unfortunately for Mr. Gore, dubbed it the Gore tax.

I am proud to welcome my friends and fellow sponsors of the bill, Representatives Tancredo and Weller, to testify before the committee this morning. I am also pleased to welcome our second panel of witnesses who will be composed of Mr. Christopher Wright, the General Counsel of the FCC; Kelly Levy, Acting Associate Administrator, Office of Policy Analysis and Development of the NTIA; and Lois Gerber, Chairman of the Board of the National Independent Private Schools Association; and Cheryl Parrino, I am trying to get the names right, CEO of Universal Service Administration Company; and Kent Lassman, Deputy Director of Technology and Communications for Citizens for a Sound Economy.

Again, let me thank my colleagues for coming. I am going in a second welcome my friend and colleague from Massachusetts, ranking member of our subcommittee, Mr. Markey for an opening statement, but we do deeply appreciate when colleagues of ours take time out to come and talk to us about issues before our committee, and we welcome you two gentlemen in particular. Mr. Markey is recognized.

Mr. MARKEY. This is such an incredibly important subject for us to be discussing, and it is one of the things that I am proudest of in terms of telecommunications policy. We included this language in the 1993, 1994 Telecommunications Act that passed the House 423 to 4. Unfortunately, that bill then died in the Senate and we had to come back and go through it again in 1995 and 96.

The key, of course, is for us to recognize that the world has just fundamentally changed since 1900. In 1900, only 7 percent of 17-year-olds had high school diplomas, and yet the people who were in leadership in our country at that time decided to build a vast network of primary and secondary schools with the intention of educating every person in our country.

Just think about that. From all the way from the Garden of Eden to 1900, five millennia, we were up to 7 percent of the population with a high school diploma. And yet this bold generation said for Irish, Italian, Poles, Jews, regardless, we have to build a school system for them.

Mr. TAUZIN. Cajuns.

Mr. MARKEY. Cajuns. Everyone. And what happens today is that 60 to 70 percent of the children in the United States graduating from high school this year are going on to college. Not high school

now, not 7 percent high school, but 60 to 70 percent college. What a transformation. What a commitment to public education.

But the jobs in 1900 were industrial. Jobs for the 21st century will be informational. They will, in fact, relate to a skill set that is not available right now, unfortunately, to the lowest income groups.

In fact, NTIA in doing a study on this subject found that there not only is a digital divide but there is a racial ravine for on-line access, the rates for whites are nearly three times as high for blacks—for whites as they are for blacks and Hispanics.

Now, the interesting thing is that by the year 2030, 50 percent of all the children in the United States will be minorities. So if we want to have an economy, an Information Age economy, a new economy, it is going to be largely populated by workers who are minorities. And so the key for us to make sure that Medicare and Social Security do have proper funding for the white baby boomers, for all baby boomers 20 and 30 years from now is if we give a good Information Age education right now to every minority. And we cannot allow this gap to open up because otherwise the jobs will go overseas. That is the core thought behind the E-Rate.

And for those of us who are Democrats that voted for GATT and NAFTA, as I did, and there are only five of us above the Mason-Dixon Line, we have a deal. Yes, we are going to have more trade but at the same time we have to give a skill set now to those who are in the lowest income groups to make sure that they have a skill set that comports with the jobs that we are going to target in this new information-based economy.

Now the good news is that the Fifth Circuit, the Federal circuit has now upheld key components of the FCC's implementation of the E-Rate provisions, in particular rejecting arguments that universal service contributions constituted a tax. So we have already got the Federal circuit court decision on this issue. It is not a tax. It has been resolved.

So that is really great news for the millions and millions of children who come from the poorest communities in America because now they can have these hookups in their classrooms and can gain access. The communities can decide yes, we will now spend money on computers, yes, we will spend the money on teacher training, and of course that is another responsibility for us, to make sure that the money is there for teacher training so that they can integrate the traditional disciplines of education with these new technologies, so that the children in that bottom percentile are given that skill set.

I think it paints a wonderful picture for our country. It shows that we understand that we need to have global trade and at the same time give this skill set to the poorest in our society. And then everyone is a winner, including our generation, that will ensure that our Social Security and Medicare trust fund will be filled by the high-skilled employment of this generation that is hooked now in by the E-Rate to this Information Age.

So I thank you, Mr. Chairman, for holding this hearing. This is about as good a set of discussions as we are going to have this year. It really talks about the key issue of our generation. Thank you.

Mr. TAUZIN. I thank my friend. Is there additional opening statements? Anyone? Mr. Shimkus?

Mr. SHIMKUS. Mr. Chairman, just to briefly make sure that I welcome my fellow Illinoian Congressman Weller. We have been fighting on this issue for a long time. And also just to say historically in the 1900's, there was a great move to public education. That move was led by local and State governments. The Federal Government really had no role at that time, to keep things in historical perspective.

The power to tax is a power to destroy. We have heard that. If we allow our government to allow agencies to tax, subverting the will of the elected representatives of this country, where does it stop and how often does it happen?

So I think the chairman's bill, which I am a cosponsor of, is a great compromise to do a couple of things that we want to do, decrease the burden of taxation on the American public while making sure that we address the need to make sure our schools have access to high speed Internet connections, and that is why I am a proud sponsor of the bill. I appreciate the work that the chairman has done. I welcome my colleagues, both colleagues, Tom Tancredo and Jerry Weller, and I look forward to their testimony.

Mr. TAUZIN. Will the gentleman yield? I think it is important to point out that very much of what the gentleman from Massachusetts has said I agree with. There will be witnesses who disagree with both of us that the government has no business spending the money connecting the schools. I happen to agree with the gentleman and with the gentleman from Massachusetts. We do have some business doing that. How we do it, who raises the tax and how it is spent is what is at issue here.

And what we have done collectively is to offer a better administrative solution and a better legal structure under which taxation of phone bills can occur to support this kind of a process. And the gentleman is absolutely correct about our concern about Federal agencies like the FCC and the very strained interpretations like the Fifth Circuit saying that a tax is not a tax when everybody who got their phone bill—my wife particularly last week said what is this new tax on the bill? And I had to explain that the FCC and the Fifth Circuit in New Orleans said it was okay. And she said you didn't actually vote on the tax increase? And I said no, we didn't. The FCC had some mysterious language that they interpreted to give them that right.

Mr. MARKEY. Will the gentleman yield?

Mr. SHIMKUS. I think my time is up, but I am happy to yield.

Mr. MARKEY. The Fifth Circuit ruled that it is not a tax. You have to call it the Gore universal service contribution. It is not the term—

Mr. SHIMKUS. I can use that. I can run with that.

Mr. MARKEY. That is the accurate description.

Mr. TAUZIN. But like Gore, that is such a boring description.

The gentleman is recognized.

Mr. SAWYER. Thank you, Mr. Chairman. I really appreciate very much the comments of all three of the members who have spoken prior to me. Let me just mention, though, that we talk about where we will be in 2030. The truth of the matter is that while we often

think of the baby boom generation as the largest population bulge ever to move through this Nation, the truth is that the current enrollment in school has for the last 1½ years beaten the record that was set by the baby boom at their height for school enrollment and will continue to beat that record for the next 12 to 15 years at minimum.

And as a result, we have a window of opportunity here in which to deal with exactly the kinds of concerns that the chairman and the ranking member have been talking about with regard to elevating the skill level of an entire Nation.

It is rare that you have the opportunity to move the aggregate skill level of, well, I guess it depends on how we count, but 265 to 275 million people in the country at once. The last time we did this actually was at the turn of the century and the 35 years before that where, in fact, there was a Federal role in education when a Republican from Vermont by the name of Justin Morrill, first in the House and then in the Senate, put together an arrangement whereby the territory that was ceded to the railroads to expand the Nation and to grow a new kind of country where a portion of those lands that were given to the railroads to increase commerce across this continent was set aside for the creation of a new kind of higher education institution. And from that grew the land-grant colleges. And instead of having simply 40 or so institutions largely for the sons of the well-to-do in this country of classical education, schools that taught business and industry and science and the practical skills of nation building grew in this Nation and it changed the face of America. I would submit that it is arguable that the 20th century in America was a product of Justin Morrill's vision.

This is a very similar kind of undertaking. It is very similar. It involves almost exactly the same set of principles and our job and what this bill is all about is trying to make those principles work right. It is not whether or not we should be involved in doing this. This gives all the control that a local community needs. It sends the dollars where they most need to go, and I think that is important. We can talk about this as it goes on, but I appreciate the comments of the gentleman and I just hope that we can keep them into some kind of perspective.

I appreciate this effort to provide a more stable funding platform for that undertaking. I am concerned about what happens to the dollars that we have been counting on for scoring purposes and how we offset those once those dollars go away. I hope we can talk about that.

I am appreciative of the effort that the FCC and the Department of Education have made to work together to make sure that these dollars do go where they most need to go. And I hope that we can ensure that the NTIA will have a similar kind of sound substantive relationship with education policy, although it is clear that they would have to control the flow of the funds.

And finally, Mr. Chairman, if I could, let me mention one element that I never hear talked about. In the struggle that we had over school safety in recent years, at no time more intensely than this year, it seems to me that there is one opportunity that we have overlooked when we talk about school guards and metal detectors and all the other kinds of changes that can be brought to



schools. It seems to me that one of the most fundamental kinds of security investments that we can make is to make sure that every classroom is no longer isolated from every other classroom as they are in American schools. The use of the wiring that goes into schools to connect hardware, not only with an electrical outlet but with the world of information, could also be used to connect classrooms with the school office via telephone.

Mr. TAUZIN. Will the gentleman yield?

Mr. SAWYER. I would, but let me just say this, it is a terribly important element in assuring the security of individual classrooms. And while we know that there have been decisions about the kinds of equipment that can be bought, including modems and all that sort of thing, it seems to me if we might make a specific reference to that in the course of this bill it could go a long way toward allowing investments of the kind that for a song, a fraction of the cost of metal detectors could go a long way toward improving classroom security.

Mr. TAUZIN. First, we ought to give some real credit to the Cellular Telephone Industry Association, which has a program like Cable in the Classroom designed to provide mobile equipment exactly for that purpose to teachers in the school buildings and in the schoolyards of America. And I think they deserve a lot of credit for their voluntary efforts in that regard.

But also I want to point out to the gentleman wireless technology, not wired technology but wireless technology, and in particular some of the new technology. Yesterday Larry Forlsom was in town, the guy who was the inventor of this new ultrabroadband technology, which has a big technology summit on in Washington today, may offer even greater security than spending all of this money to rewire the insides of school buildings.

One of the concerns we have in our bill is this effort to focus on a single form of technology when there may be other less expensive, much more competent technologies to accomplish those purposes, but the gentleman is exactly right. Communications inside the school can vastly increase school safety and it is one thing we need to focus on.

Mr. SAWYER. I agree with everything you said. Thank you, Mr. Chairman.

Mr. TAUZIN. Further opening statements?

[Additional statements submitted for the record follow:]

PREPARED STATEMENT OF HON. MICHAEL G. OXLEY, A REPRESENTATIVE IN CONGRESS  
FROM THE STATE OF OHIO

Thank you, Mr. Chairman, and welcome to our witnesses.

As we all know by now, the FCC's program to wire all of the nation's two million classrooms and 16,000 libraries directly to the Internet has led to a new tax on consumers.

Allegedly based on provisions of the Telecommunications Act of 1996 calling for discounted telephone line rates for schools and libraries, the concept of service discounts has been expanded beyond recognition into a multi-BILLION dollar grant program.

While I support efforts by local school districts to wire classrooms for Internet access if they so desire, and I have no objection to the concept of discounted telecommunications rates for educational institutions, I object strenuously to the FCC's perversion of congressional intent and self-anointed role as tax collector for this electronic white elephant sale. Upwards of 80 percent of schools are already connected

to the Internet, thanks to school board and private-sector initiatives. The Gore Tax is unnecessary. The only purposes it serves are political.

Under pressure from consumers and Congress, including this Member, the FCC initially voted to cut the program approximately in half and agreed to reform some of the more objectionable aspects of its implementation. However, the Commission later reversed course and ordered “full” funding of the Gore Tax program to the tune of \$2.25 *billion*. I am of the firm opinion that this backdoor tax increase imposed by unelected bureaucrats cannot be allowed to stand.

I support the legislation before us as the minimum we should do to reign in an agency run amok. I also believe this case study confirms the need to reform the FCC and impose some discipline and more attention to congressional intent.

Thank you, Mr. Chairman. I yield back.

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PREPARED STATEMENT OF HON. BARBARA CUBIN, A REPRESENTATIVE IN CONGRESS  
FROM THE STATE OF WYOMING

Thank you, Mr. Chairman, for holding this very important legislative hearing on the bill H.R. 1746, the *Schools and Libraries Internet Access Act*.

As a recent cosponsor of your legislation, I would like to commend you on your thoughtfulness in putting together this bipartisan, well crafted, and responsible bill.

For the past two years I have continually gotten comments from angry constituents who are enraged about the federal charges on their phone bills.

Today phone bills look more like tax statements than they do utility bills.

H.R. 1746 would address this two-fold. First it would repeal one of the federal charges by replacing the FCC’s existing schools and libraries program. Second, it would repeal altogether the three percent excise tax on October 1, 2004.

Until the 2004 sunset of the excise tax, one percent of the tax would go toward funding the telecommunication services to qualified schools, libraries and rural health care providers.

One of the most attractive things to me about H.R. 1746 is that it allows the funds to be allocated to all 50 states and used according to the states’ plans.

This effectively gets the federal government—namely the FCC—out of dictating how these monies should be spent and alleviates the uncertainty that the FCC could adjust, modify or eliminate altogether the funding mechanism.

Let me be clear about one thing: schools, libraries and rural health care providers deserve to have the best advanced services available.

H.R. 1746 would provide a tremendous amount of resources to enhance schools’ and libraries’ access to advanced telecommunications and information services.

Mr. Chairman, I once again applaud your work on putting together this very important piece of legislation. I look forward to hearing from today’s witnesses and look forward to one day seeing this bill become law. I yield back the balance of my time.

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PREPARED STATEMENT OF HON. TOM BLILEY, CHAIRMAN, COMMITTEE ON COMMERCE

Thank you Mr. Chairman. I am anxious to hear the views of our esteemed panel this morning on the Federal program that provides telecommunications services to schools, libraries and rural health care providers. I particularly would like to welcome my colleagues, Representatives Tancredo and Weller, to the Commerce Committee this morning to share their views on this important issue.

Mr. Chairman, I think it is safe to say that no one on this panel, or around this entire country is opposed to having schools provide the best education and information possible to children. As we move at rapid speed into a digital arena, we should offer the most up to date service and technology to as many U.S. citizens as possible. That said, I do think rational minds disagree as to the best way to achieve this worthy goal.

The program to provide these telecommunications services, sometimes called the E-RATE program, and sometimes also referred to as the “Gore Tax” is out of control. Currently there are over 2.45 billion dollars worth of requests from eligible schools, libraries and organizations. In order to meet this high level of demand, the FCC unilaterally increased the cap for this program this past summer. By doing so, the FCC not only raised the federal telephone E-Rate tax, but it also took bold steps to prevent phone companies from identifying the tax on their customers’ phone bills. Whether one agrees or disagrees with the specifics of the program, we all should agree that folks should at least know when they’re being taxed, and for what purpose.

I question why the FCC assumes that they have the authority to take such action. The 1996 Telecommunications Act does not allow the FCC to increase such a tax without Congressional approval.

In the Commonwealth of Virginia, even before the FCC doubled the tax earlier this summer, Virginians paid 50.2 million dollars during the first cycle of the Gore Tax, but in return, got back only 24.9 million dollars from the FCC. By contrast, Puerto Rico paid only 13.3 million dollars in the first cycle, **but received a whopping 47.6 million dollars in subsidies!** The Gore Phone Tax is fundamentally illegal and unfair. It's unfair to *all* consumers, and it's certainly unfair to three-quarters of the States.

I commend Chairman Tauzin for taking his initiative to address this problem with his bill, H.R. 1746, the Schools and Libraries Internet Access Act. This bill offers one possible solution which would address some of the concerns about the FCC's implementation of the program.

I look forward to hearing more about this legislation, as well as other possible solutions from our two panels of witnesses this morning.

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PREPARED STATEMENT OF HON. ANNA G. ESHOO, A REPRESENTATIVE IN CONGRESS  
FROM THE STATE OF CALIFORNIA

Because of a markup in the Health and Environment Subcommittee, I cannot attend this hearing on H.R. 1746, the *Schools and Libraries Internet Access Act* this morning.

I'm troubled by the implications of H.R. 1746. The legislation would revamp funding for the e-rate, slashing the 3% federal communications excise tax by two-thirds and reallocating the remaining revenue to fund the e-rate. This means a significant reduction in funds to schools and libraries who need these funds to wire their schools to the Internet.

In addition to funding the wiring of schools and libraries, this program offers schools and libraries a discount in the cost of accessing the Internet.

H.R. 1746 would sunset all funding in the year 2004. This means that schools and libraries would no longer receive a discount. Our nation's schools and libraries are already overburdened by the costs associated with educating our children, and this legislation would be another burden for them to shoulder.

This bill kills the e-rate. Republicans supported the e-rate when it was included in the 1996 Telecommunications Act and now the same Republicans are bashing it.

The funding mechanism for the E-rate was part of the Telecommunications Act of 1996 and was passed in the House on a bipartisan vote of 414-16 and 91-5 in the Senate. *Not one House Republican voted against the Act.*

We should support full funding of the e-rate program and here's why:

- The E-rate works. The E-rate program is playing a pivotal role in bringing technology into our children's lives. The program is making computers in the classroom the rule, not the exception. Because of the E-rate we're closer to the day when children, their parents and their teachers will walk into a classroom filled with computers linked to the Internet, and not give it a second thought.
- In just 18 months, the E-rate has connected over 600,000 classrooms in over 80,000 schools and libraries across America. If the FCC funds the E-rate at \$2.25 billion, the E-rate will connect an additional 528,000 classrooms. For most schools and libraries, the cost of both telephone and Internet access will be cut in half. For some of our poorest schools, access will be almost free.
- The E-rate is helping our country close the digital divide. Because of the E-rate, children in the most isolated inner city or rural town will have access to the same universe of knowledge and technology as a child in the most affluent suburb. The schools hurt most by attempts like H.R. 1746 to slash the E-rate will be schools in rural America.

The Education Department has found that smaller and economically disadvantaged schools are now just as likely to have Internet connections as larger, wealthier schools. The survey also found 80 percent of the poorest schools have Net connections as of 1998, compared to 87 percent of the wealthiest schools. But at the classroom level, the poorer schools still lag in connectivity, with only 39 percent online.

Access to technology doesn't guarantee our children will succeed, but lack of technology guarantees our children will fail. For America to ensure that our children have a shot at the American dream, we must have computers in the classroom. The E-rate makes that goal more attainable.

If our children do not have the technological resources they need to compete in an ever-changing global information economy, our nation will be poorer for it. The

E-rate provides students more access to educational technology and empowers them with the tools they need to succeed in the Information Age.

Being literate today means not only being able to read, but possessing computer skills. Technological literacy and ongoing access to information technology resources is essential, and for many school-aged children and adults, our schools and libraries may be their only opportunity to access and use a networked computer.

The American Electronic Association recently released a study that shows while math and science test score levels have improved since 1990, fewer and fewer students are receiving degrees in either math or science.

If America is going to keep competing and winning in this global economy, more of our children must choose careers in math or science. By putting computers in the classroom, the E-rate is helping to produce the next generation of scientists and mathematicians.

I'm disappointed the Commerce Committee schedule prevents me from attending this hearing. I'm confident that the testimony will be useful in demonstrating how successful this program is and that there is absolutely no need to destroy the funding mechanism of a successful effort.

Mr. TAUZIN. The Chair is pleased to welcome our guests on the first panel. The Honorable Jerry Weller and the Honorable Tom Tancredo. Jerry, you can begin. We have a 5-minute rule but we are flexible. We appreciate your testimony.

**STATEMENT OF HON. JERRY WELLER, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ILLINOIS**

Mr. WELLER. Thank you, Mr. Chairman, Mr. Markey, and the members of the subcommittee. Thank you for the opportunity to testify today on an important issue. I come before the subcommittee as a strong supporter of our Nation's goal of ensuring that every child in America has access to the Internet and computers through our local libraries as well as our local schools. And the reason is I believe in the 21st century knowledge and understanding of the Internet is a basic skill not only at home but in the workplace and we should ensure that every American child should have this opportunity and I think we all could agree on that in a bipartisan way. And that is why I appreciate the opportunity to testify today.

I particularly also want to thank Chairman Tauzin for your leadership and the opportunity to work with you on legislation which we all believe will bring stability as well as legitimacy to an important program providing Internet access to local schools and libraries not only through access discounts but the installation of the wire, the fiber and the hardware in our local schools and libraries. Our work on this bill began as an effort to achieve a goal we all share, which is giving every American child access to the Internet. And when we passed the Telecommunications Act in 1996, it included a simple directive that any telecommunications carrier serving a particular geographical area must make any of its services under the universal service fund, USF, available at reduced rates to schools and libraries.

Unfortunately, the FCC misinterpreted the Telecommunications Act and they have jeopardized the goal that we all share, which is providing Internet access for all of America's children.

First the FCC determined that as much as \$2,250,000 in funding should be made available to support universal service to schools and libraries. Second, the FCC expanded the scope of what was available for schools and libraries from just discounted rates on telecommunications services and decided to include Internet access

costs and Internet connections, which essentially is the wire, the fiber, and the hardware.

Third, the FCC created a whole new bureaucracy known as the School and Library Corporation to administer the Internet access program without authorization from Congress to do so. Finally, probably the mostly questionable of all the provisions, the FCC determined that the funds supporting the Internet access for school and libraries should come from a tax on all long distance telecommunications service providers.

Here are the problems we are now facing: FCC has taken unauthorized action to create a new bureaucracy to administer a program whose funding base may not be secure and, second, the FCC has taken the act of imposing an unauthorized tax on telephone users in order to cover the expense of this enterprise.

The FCC is incorrect in its contention that this unauthorized tax is a fee. A fee is a charge for a service rendered. However, long distance users are not receiving a service. Thus, if a charge is levied and no direct service is provided, then it is characterized as a tax regardless of whether it shows up on your 1040 form or your telephone bill. And only Congress under our Constitution can impose a tax.

As a member of the House Ways and Means Committee which has jurisdiction over tax issues, I believe this position taken by the FCC is wrong. Today many schools and libraries across this country have come to depend and look to the Internet access program as a source of funding. And of course this funding source, as we recognize it, is not secure, which means neither are their technology programs.

In the district that I represent local school districts have received some funding. Lincoln Elementary School in Calumet City received over \$51,000. Marseilles Elementary school received over \$22,000. La Salle Bruton High School, which is over a century old, a building built like a fort, they estimate it is going to cost well over a million dollars for that school to put in the wire, the fiber and the hardware to guarantee every child access to the Internet.

These and other schools across the country deserve to know that their Internet access funding is secure. The fact of the matter is the FCC implemented a program based upon a funding source that many Members of Congress believe they did not have the right to utilize.

Congress, not the FCC, is the only body under our Constitution authorized to impose a tax. Chairman Tauzin and I want to fix this problem by ensuring that a funding source for school library Internet access is secure. The Schools and Library Internet Access Act would protect the technology assistance programs for the over 1,800 schools in Illinois alone by slashing the World War I, 3 percent telephone excise tax currently sent to the general treasury, to 1 percent and earmarking this remaining revenue to fund this important schools and library Internet access program through block grants to the States. In addition the slash in the current tax, the Schools and Libraries Internet Access Act would repeal the 3 percent unconstitutional tax on long distance customers.

Our legislation would save consumers \$5 billion while providing over \$1.7 billion in the first year to equip our Nation's schools and libraries with Internet access.

The legislation effectively kills two birds with one stone. First, the legislation preserves and expands funding for the important Internet access assistance programs to our schools and libraries and places it appropriately under the jurisdiction of the National Telecommunications and Information Administration. Second, the legislation abolishes the FCC's taxing mechanism and reduces an antiquated World War I tax which disproportionately impacts the poor and our Nation's senior citizens while guaranteeing a revenue stream of anywhere from \$1.7 to \$2 billion a year for Internet access to our schools and libraries.

We believe we can do it right this time. This legislation corrects the problem. The FCC and its tax created the problem. However, we all sit here today in support of the bipartisan goal of giving every child in America through their schools and libraries access to the Internet. And we believe we need to solve this problem by enacting the Schools and Libraries Internet Access Act. It is the right thing to do. Let's work in a bipartisan fashion and get it done. Therefore, I ask my colleagues on this subcommittee as well as members of this committee and the full House and Senate, to give the Schools and Library Internet Access Act favorable consideration.

I look forward to working with you. Thank you for the opportunity to testify.

[The prepared statement of Hon. Jerry Weller follows:]

PREPARED STATEMENT OF HON. JERRY WELLER, A REPRESENTATIVE IN CONGRESS  
FROM THE STATE OF ILLINOIS

First, let me thank you for the opportunity to work with you on this important legislation which will bring stability and legitimacy to an important program which provides Internet access to local schools and libraries through access discounts. I appreciate the opportunity to testify here today.

Our work on this bill began as an effort to achieve a goal we all share...giving every child access to the Internet through our local schools and libraries.

When we passed the Telecommunications Act of 1996, it included a simple directive that any telecommunications carrier serving a particular geographic area must make any of its services under the Universal Service Fund (USF) available at reduced rates to schools and libraries. Unfortunately, the FCC misinterpreted the Telecommunications Act and may have jeopardized the goal we all share, which is providing Internet access for all of America's children.

First, the FCC determined that as much as \$2.25 billion per year should be made available to support universal service for schools and libraries. Second, FCC expanded the scope of what was available for schools and libraries from just discounted rates on the telecommunications services and decided to include Internet access costs and internal connections (wiring). Third, the FCC created a whole new bureaucracy, known as the School and Library Corporation to administer the e-rate program without authorization from Congress to do so. Finally, with probably the most questionable of all of the provisions, the FCC determined that the funds supporting the e-rate, for schools and libraries should come from an assessment, or tax, on all long distance telecommunications service providers.

Here are the problems that we now face: 1) The FCC has taken unauthorized action to create a new bureaucracy to administer a program whose funding base may not be secure 2) The FCC has taken the unconstitutional action of imposing an unauthorized tax on long distance users in order to cover the expense of this enterprise.

The FCC is incorrect in its contention that this unauthorized tax is a fee. A fee is a charge for a service rendered; however, long distance users are not receiving a service. Thus, if a charge is levied and no direct service is provided then it is char-

acterized as a tax, regardless of whether it shows up on your 1040 form or your telephone bill, and only Congress can impose a tax under the Constitution. The FCC's actions are being contested in court.

The result is that many schools across the country have come to depend and rely on the E-Rate program. Without a secure funding source, their technology programs may be in jeopardy. Some examples in the 11th District of Illinois which I represent, Lincoln Elementary School in Calumet City, Illinois received \$51,214 for internal connections and Internet access; Marseilles Elementary School received \$22,055 for internal connections.

These and other schools across the country deserve to know that their E-rate is secure. The fact of the matter is, the FCC implemented a program based upon a funding source that is unconstitutional. Congress, not the FCC, is the only body able to impose a tax. Chairman Tauzin and I want to fix this problem by ensuring that the funding source for the erate program is secure.

The Schools and Library Internet Access Act would protect the technology assistance program for over 1,800 schools in Illinois alone by slashing the World War I three percent telephone excise tax (currently sent to the general fund) to 1% and earmarking the remaining revenue to fund the important school and library Internet access programs through block grants to the states. In addition to slashing the current tax, The Schools and Library Internet Access Act would repeal the 3% unconstitutional Tax on long distance customers. Our legislation will save consumers \$5 billion while providing \$1.7 billion in the first year to equip our nation's schools and libraries with Internet access.

The legislation effectively kills two birds with one stone. First, the legislation preserves and expands funding for the important Internet access assistance program to our schools and libraries and places it appropriately under the jurisdiction of the National Telecommunications and Information Administration. Second, the legislation abolishes the FCC's unconstitutional funding mechanism and reduces an antiquated World War I tax which disproportionately impacts the poor and senior citizens.

Let's do it right this time. The FCC and its unconstitutional tax created the problem. However, I support the bipartisan goal of giving every child in school access to the Internet and believe we need to solve this problem by enacting The Schools and Library Internet Access Act. It is the right thing to do. Lets work in a bipartisan fashion to get it done.

Therefore I ask my colleagues to give the Schools and Libraries Internet Access Act favorable consideration in this committee.

Thank you, Mr. Chairman

Mr. TAUZIN. Thank you, Mr. Weller, and now the Honorable Tom Tancredo from Colorado.

#### **STATEMENT OF HON. THOMAS G. TANCREDO, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF COLORADO**

Mr. TANCREDO. Thank you, Mr. Chairman. I want to thank you for the opportunity to testify on H.R. 1746, the Schools and Libraries Internet Access Act, and appreciate the forum that you have provided to discuss the problems that frankly I believe to be inherent in a bizarre and incredibly complex world of telecommunications taxation.

As an original cosponsor of this bill, I look forward to seeing its passage in the near future. The Schools and Library Internet Access Act goes a long way toward bringing some degree of relief to the confused and overtaxed phone customer. Simply trying to decipher the typical charges on one's phone bill today requires an analysis of a perplexing array of charges that defy easy explanation or a defensible rationale.

Mr. Chairman, your bill could be called the telephone taxpayer's Bill of Rights as it epitomizes three cardinals of good tax policy: Simplicity, accountability and fairness, I believe all three are lacking in the present—and I sort of hesitate to use the word—system.

I brought with me a constituent's phone bill from this last February, and I think it illustrates the point perfectly. We have since received many similar in nature. In the course of 1 month the gentleman from Lakewood, Colorado, made a 1-minute phone call to Minneapolis costing 15 cents. As you will see by the facsimile of the bill that he sent me, he had \$1.84 in taxes and charges on that 15-cent phone call. He was confused about this, of course. He thought that he might be actually paying \$1.84 in taxes for every minute he spent on the phone. I don't know what it did to his long distance dialing from that point on and access, but it certainly probably scared him to a certain extent. I can only imagine that he has not used his long distance since then, at least to any extent.

Although we can try to explain to the best of our ability what these charges were for, and of course he would face many of these inexplicable charges regardless of his calling frequency, at least the way this particular company, AT&T, chooses to bill for it. Other companies bill differently. They do bill as a result of a percentage of your usage. In this case, this company does not.

To recover the costs of the universal service fund which funds the schools and libraries E-Rate program as well as other more traditional universal service programs, this gentleman's long distance phone company charged a flat rate of 93 cents per customer. Add on the 85 cents line charge for local service providers and the almost 100-year-old 3 percent telecommunications excise tax, the total is \$1.99.

Unfortunately, like all overtaxed phone customers, my constituent remains a victim to the whims of the FCC. In May of this year without so much as the expressed consent of Congress, the FCC raised the E-Rate tax by \$600 million. The Wall Street Journal estimated that the increase could amount to an additional 40 cents per month on the average bill. The FCC's abilities to raise this tax has slipped through the cracks of the 1996 Telecommunications Act and more recently through the Federal judicial system, I think. It remains largely unaccountable for the way it levies these charges on a day-to-day basis. There is no doubt in my mind that the FCC will appear before the Congress next year demanding statutory increases above the \$2.25 billion cap on the E-Rate program.

The first bill I introduced into the Congress was H.R. 692, the E-Rate Termination Act, to end the FCC's program entirely. I have consistently referred to the E-Rate program as a tax because I believe it meets the criteria of a tax. I certainly believe that my constituents, and this particular customer, would think of all those charges as a tax. I guess I could explain to them that they really are not a tax, that the FCC said they are not a tax, that the Court says they are not a tax. I don't really know whether or not he would believe that this thing that waddles, quacks and has feathers is anything but the duck that it really and truly is. It is a tax.

By levying the charge on telecommunications companies that will not participate in providing services to schools and libraries, the FCC has extended the intent of the 1996 Telecommunications Act. Testifying before the Ways and Means Committee, Commissioner Harold Furtchgott-Roth explains that quote: A tax confers no special benefit on the payee, is intended to raise general revenue, and



is imposed for some public purpose. In contrast, a fee is a payment for a voluntary act such as obtaining a permit.

Certainly the E-Rate program is not voluntary and the Congressional Budget Office has determined that all universal service contributions, including E-Rate contributions, should be treated as Federal revenues.

The Schools and Libraries Internet Access Act will fund the E-Rate program in a more honest fashion by eventually bringing the program into the general fund where it can be subjected to the annual scrutiny of the congressional appropriators.

Simplicity, accountability, fairness. Americans who support these principles in our tax policy should support the Schools and Libraries Internet Access Act, and I should say also, Mr. Chairman, that I am fully aware of the altruistic motives that were—that motivated the Congress of the United States in the adoption of the original legislation, and I am not arguing with them at all. But regardless of how altruistic they were, we have to recognize that some problems may exist because they were—because the bill developed in a vacuum to a certain extent. It developed without a lot of discussion about what was going on in this particular area to begin with. How many programs were we funding in the Federal Government for technology in the public schools?

I am on the Committee on Education and the Workforce. The Secretary of Education came before our committee and I asked him specifically that question: How much are we doing just in the Education Department? How many programs do we actually use to fund technology in the schools? He said he was not sure. I said do you have any idea how many programs that other agencies are involved with? He said he was not sure but he would get back to us on that. He never has up to this point in time.

The fact is when it is as uncoordinated as this is, to add another program of this nature, again no matter how altruistic in nature, could be counterproductive if we do not know what the government is doing in total, if we do not know exactly what is being collected and spent for the technology in classrooms and how that money actually produces some sort of change in classrooms.

And we also make a—it is sort of a—well, an assumption about the present system, the present sort of industrial model educational system that we have in America as being the one we are going to have for throughout the next century and the one most able to accept this technology and deal with it successfully. And I suggest to you that we really don't know that this industrial model system where you have one building brick-and-mortar facility, all kinds of kids coming in the morning, all kinds of adults to meet them for 6 hours a day 184 days a year inside this facility and we call that education. We don't know if that will really be the way we will be educating children in the next century.

But we have made an assumption about that when we built the process into this particular piece of legislation or in the original Telecommunications Act. It is something I think that needs to be fixed and I thank you again, Mr. Chairman and members of the committee, for the opportunity to voice my support for this bill.

[The prepared statement of Hon. Thomas G. Tancredo follows:]

PREPARED STATEMENT OF HON. THOMAS G. TANCREDO, A REPRESENTATIVE IN  
CONGRESS FROM THE STATE OF COLORADO

Good morning Mr. Chairman and Members of the Committee. I thank you for the opportunity to offer testimony on H.R. 1746, the Schools and Libraries Internet Access Act and appreciate the forum you have provided to discuss the problems I believe to be inherent in the bizarre and incredibly complex world of telecommunications taxation. As an enthusiastic original cosponsor of this bill, I look forward to seeing its passage in the near future.

The Schools and Libraries Internet Access act goes a long way toward bringing some degree of relief to the confused and overtaxed phone customer. Simply trying to decipher the typical charges on one's phone bill today requires an analysis of a perplexing array of charges that defy either easy explanation or a defensible rationale.

Mr. Chairman, your bill could be called the Telephone Taxpayer's Bill of Rights as it epitomizes three cardinal principals of good tax policy—simplicity, accountability, and fairness. I believe all three are lacking in the present "system."

*Simplicity*

I have brought with me a constituent's phone bill from this past February that I think illustrates this point perfectly. In the course of one month, this gentleman from Lakewood, Colorado, made only a one-minute phone call to Minneapolis costing 15 cents, and as you will see by the facsimile of the bill he sent me, he believed he was charged what is essentially \$1.84 in taxes and charges. In his confusion over these charges, he feared he might be charged \$1.84 in taxes for every minute he spent on the phone! I can only imagine that this poor man has not used his long distance service since!

A closer examination of his phone bill shows that he would face many of these same inexplicable charges regardless of his calling frequency. To recover the costs of the universal service fund, which funds the Schools and Libraries E-Rate Program as well as other, more traditional universal service subsidies to rural areas, this gentleman's long distance phone company charged a flat rate of 93 cents per customer. Add on the 85 cents line charge for local service providers, and the 100-year-old three percent telecommunications excise tax, and his total bill was \$1.99.

The Schools and Libraries Internet Access Program would help Americans like my constituent from Lakewood by immediately reducing, and eventually phasing out the telephone customer excise tax, and by bringing the charges associated with the E-Rate Program in to the Treasury, and eventually on budget. No longer will the FCC have the ability raise his taxes through this program, and no longer will he be assessed a 100 year old federal tax originated as a luxury tax to fund the Spanish American War.

Simplicity, my colleagues, is the message we want to support here, and that the Schools and Libraries Internet Access Act moves toward. Simplicity—not only in light of the myriad of taxes and surcharges that deluge a phone customer—but also in the way we manage our funding for the technology that schools receive. In a hearing before this Subcommittee last year, the Government Accounting Office estimated that at least 27 federal programs provide funding that may be used to purchase this technology for Schools and Libraries. For three of these programs that specifically target funding for technology in schools and libraries, the President requested a funding level of more than \$1 billion for Fiscal Year 2000.

As a member of the Education Committee, I am delighted that this bill returns the control of technology funding in schools and libraries to the nation's elected officials. There is much work to be done in the Education Committee on this front. Of course, I find it ironic that the only intriguing argument I have heard in favor of the program as it currently stands, is that it is probably better managed than if it were run under the Department of Education. Again, that is another matter that Congress must address.

*Accountability*

Americans deserve to hold their federal agencies, and Congress, accountable for the money spent on technology funding in schools and libraries. Moreover, they deserve accountability for the charges they pay on their phone bills.

In a recent testimony before the Senate Committee on Commerce, FCC Commissioner Harold Furchtgott-Roth lamented that the FCC has made little progress in addressing the problems that plague the E-Rate program highlighted by the GAO in 1998 and denounced by many members of Congress. In March of 1999 the GAO published a progress report on the E-Rate program, riddled with evidence of poor, if any, accountability for the issuance of discounts. Specifically, the GAO stated that the FCC has not yet implemented the GAO's recommendation to cite adequate

goals, performance targets, and measures for the program. It also cited a serious concern that too many schools were issued inappropriate discounts, and that an increasing number of such problems may occur if this program continues.<sup>1</sup>

In May of this year, without so much as the expressed consent of Congress, the FCC raised the E-Rate tax by \$600 million. The Wall Street Journal estimated that the increase could amount to an additional 40 cents per month on the average bill.<sup>2</sup> The FCC's ability to raise this tax has slipped through the cracks of the 1996 Telecommunications Act and more recently through the federal judicial system. It remains largely unaccountable for the way that it levies these charges on a day to day basis.

There is no doubt in my mind that the FCC will appear before Congress next year demanding a statutory increase of the \$2.25 billion cap on the E-Rate program. Throughout the course of time that the FCC has so zealously fought for billions in E-Rate funding, it has delayed its consideration of revamping the more traditional channels of universal service funding, particularly those programs serving rural Americans.

Mr. Chairman, the first bill I introduced in Congress was H.R. 692 The E-Rate Termination Act, to terminate the FCC's program entirely. I introduced that bill on the same day that the House passed the Mandates Information Act, which will serve as a warning flag within bills we consider that may cause unfunded mandates on the private sector and consumers. This program is not only an unfunded mandate, it is an uncontrolled one, and Americans deserve more accountability.

#### *Fairness*

The Schools and Libraries Internet Access Act will eliminate and phase out the E-Rate tax and the telephone customer excise tax, respectively. This is a measure of fairness for both taxpayers and the many telecommunications companies that currently contribute to the E-Rate Fund, a back-door tax masked with ludicrous misnomers such as a "Mandatory Contribution."

I have consistently referred to the E-Rate Program as a "Tax" because I believe it meets the criteria of a tax rather than that of an administrative fee or charge. By levying the E-Rate universal service charge on every interstate telecommunications company, the FCC has exceeded the intent of the 1996 Telecommunications Act by charging companies, such as wireless phone companies, that will not see a financial return by providing services to schools and libraries. Testifying before the Subcommittee on Oversight of the House Committee on Ways and Means on August 4, 1998, Commissioner Furchtgott-Roth stated the following:

In general, taxes can be distinguished from administrative fees by determining the recipient of the ultimate benefit: a tax "confers no special benefit on the payee," "is intended to raise general revenue," or is "imposed for some public purpose." In contrast, a "fee" is a "payment for a voluntary act, such as obtaining a permit." As the Supreme Court has held, and the D.C. Circuit further explained, a "fee" is a payment "incident to a voluntary act, e.g., a request that a public agency permit an applicant to practice law or medicine or construct a house or run a broadcast station. The public agency performing those services normally may exact a fee for a grant which, presumably, bestows a benefit on the applicant, not shared by other members of society."

Here, all these factors point toward the category of a tax: the fund, which creates internet access for schools and libraries, confers no particular advantages upon telecommunications carriers in exchange for their contributions, such as a license or permit; the funds have not, as far as I can tell, been segregated from other government monies; the purpose of the fund is a broad, social one, purportedly to improve education for all Americans; and the payment requirement is not triggered by a voluntary act on the part of telecommunications carriers, such as the filing of an application, but is a flat mandate.<sup>3</sup>

Therefore, the current E-Rate program is funded by a backdoor tax—collected in a mandatory rather than voluntary fashion. In fact, the Congressional Budget Office has determined that all universal service contributions should be treated as federal revenues, supporting the argument that this is federal revenue generated in the form of a tax.

<sup>1</sup> GAO/RCED-99-5 1. GAO Report to the Chairman, Committee on Commerce, Science, and Transportation, U.S. Senate, March 1999, pp. 7-8.

<sup>2</sup> "Gore Tax Hike" *The Wall Street Journal*, May 12, 1999.

<sup>3</sup> The Honorable Harold Furchtgott-Roth, Commissioner, Federal Communications Commission before the House Subcommittee on Oversight of the House Committee on Ways and Means. August 4, 1998.

The Schools and Libraries Internet Access Act will fund the E-Rate program in a more honest fashion, by first establishing a trust fund program through a reduced telecommunications excise tax, and eventually bringing the program into the general fund, where it can be subjected to the annual scrutiny of Congressional appropriators. No longer will constituents pay for the E-Rate program through the funds described as a “Universal Charge” or “Mandatory Contribution.”

Finally, this bill should provide an enormous tax relief for those companies that do not see a return of business through the E-Rate program. The arbitrary and unfair charges on companies levied by the FCC to fund the E-Rate program will cease. Billions of dollars will be returned to the nation’s growing high-technology business sector.

Simplicity, accountability, and fairness. Americans who support these principles in our tax policy should support the Schools and Libraries Internet Access Act. I thank you again, Mr. Chairman and members of the Committee, for the opportunity to voice my support for this important bill.

Mr. TAUZIN. Thank you both. The Chair recognizes himself quickly. I appreciate both of your comments and the contributions. And I would like at this point to ask unanimous consent that written statements for all members be made a part of the record as well as our witnesses and also to ask unanimous consent to file under the record of this proceeding a new recent study entitled “The High Cost of Taxing Telecom,” prepared by Jeffrey Eisenach of the Progress and Freedom Foundation.

[The information referred to follows:]

#### THE HIGH COST OF TAXING TELECOM

BY JEFFREY A. EISENACH<sup>1</sup>

##### *Introduction and Summary*

Driven by technological progress, the telecommunications industry is nearing the end of a 30-year transition from natural monopoly to competitive market. Public policy has recognized this change through substantial deregulation and creation of a legal framework designed to facilitate competition. Tax policy, however, has not kept pace with the changing nature of the telecommunications business. As a result, the telecommunications industry is subjected to a vast array of taxes that have no apparent justification in the modern era and can be explained solely as holdovers from all but forgotten era. Simply put, there are too many taxes on telecommunications services, and they are far too high.

Taxes on telecommunications are, inevitably, taxes on the Internet. Whether through dial-up access or Digital Subscriber Lines (DSL), over cable modems or wireless ones, access to the Internet takes place over the telecommunications network. Thus, high telecommunications taxes slow the spread of Internet access and discourage deployment of the broadband networks needed for the next generation of Internet growth. They raise the costs of electronic commerce for every business, big or small, and raise the price of Internet access for every household, rich or poor. Their impact is probably greatest, however, on poor households, small businesses and rural communities.

The convergence of previously separate telecommunications technologies—cable, telephone, satellite, wireless—into a single marketplace adds further urgency to the need for telecommunications tax reform. Each of these different industry sectors is subject to its own tax regime, meaning that the same service can be subject to very different tax treatment depending on the type of firm that offers it, and efforts to eliminate such consistencies are hampered by the extreme complexity of the system.

This paper represents a first step in an effort to reassess and to recommend reforms in telecommunications taxes. It describes the current regime and presents very preliminary findings about the impact of current policies in terms of both eco-

<sup>1</sup>Jeffrey A. Eisenach is president and co-founder of The Progress & Freedom Foundation. The views expressed here are his own and do not necessarily reflect those of The Progress & Freedom Foundation, its officers or Board of Directors.

conomic efficiency and fairness. The paper concludes with a brief discussion of potential policy implications.<sup>2</sup>

#### *Telecommunications Taxes in the United States*

Telecommunications services in the United States are subject to an almost incomprehensible array of taxes at the local, state and Federal levels. Indeed, there are so many taxing entities levying so many taxes, fees and other charges that there literally is no comprehensive data source from which a complete listing can be obtained. Nevertheless, it is possible to paint a fairly accurate picture of the overall level of telecommunications taxes.<sup>3</sup>

**Federal Taxes:** The Federal government taxes telecommunications in three significant ways. First, it levies a three-percent excise tax on all telecommunications services. Second, it imposes fees on long-distance carriers that are used to subsidize the provision of telecommunications services, wiring and computer-related equipment at schools, libraries and rural health care centers. Third, it oversees a system of "access charges" through which long-distance phone carriers subsidize the below-cost provision of local telephone service to selected customers. Of these, only the first is universally agreed to be a "tax."<sup>4</sup>

The Federal telecommunications excise tax (FET) adds three percent to the cost of every telecommunications bill. It covers both long distance and local telephone service for both residential and business customers. Revenues from the tax are treated as general revenues. The FET is projected to raise about \$5 billion in FY 1999. As shown below, this makes it the third largest general revenue excise tax in the U.S. budget, just behind alcohol and tobacco. Nevertheless, the tax accounts for less than four tenths of one percent of Federal revenue. By comparison, the Office of Management and Budget estimates the FY 1999 Federal budget surplus at \$99 billion.

Table One:  
General Fund Excise Taxes<sup>5</sup>

Product	Revenue (FY 1998, millions)	Share of On-Budget Federal Revenue
Alcohol .....	\$7,215	0.53%
Tobacco .....	\$5,657	0.44%
Telecommunications .....	\$4,910	0.38%

<sup>5</sup> Beginning in 1998, revenues from the excise tax on motor fuels were removed from general revenues and dedicated virtually entirely to the highway trust fund. At nearly \$40 billion, the tax on motor fuels is far and away the largest Federal excise tax in terms of revenue raised. Source: Office of Management and Budget, **Budget of the United States: Historical Tables** (Washington: Government Printing Office, 1999).

Source: Office of Management and Budget

The second major tax on telecommunications services is the tax levied on long distance carriers to support the Federal Communications Commission's "e-rate" program. In May 1999, the FCC voted to raise the annual amount of this tax by approximately \$1 billion to \$2.25 billion annually.<sup>6</sup> These taxes are passed through by

<sup>2</sup> This paper was prepared for presentation to the Advisory Commission on Electronic Commerce, September 14, 1999. It presents preliminary results from an ongoing study of telecommunications taxation underway at The Progress & Freedom Foundation. All results are tentative and subject to further modification. The final study is due out in mid-2000.

<sup>3</sup> A major new study by the Committee on State Taxation (COST) provides a wealth of data on state and local taxation of telecommunications services. See Committee on State Taxation, *50-State Study and Report on Telecommunications Taxation* (Washington, DC: Committee on State Taxation, 1999). This study will make possible far more sophisticated analyses of telecommunications taxes than have been possible in the past. While the study was not completed in time for its results to be incorporated in this paper, the author wishes to thank COST for an advance copy.

<sup>4</sup> While these are the three *most* significant Federal taxes, they are by no means the only ones. Telecommunications carriers pay a wide variety of regulatory fees, participate in extremely complex cross-subsidization programs, are subject to a number of unfunded mandates and face numerous unfavorable depreciation and related provisions.

<sup>6</sup> See Federal Communications Commission, *In re: Federal-State Board on Universal Service: Twelfth Order on Reconsideration in CC Docket No. 96-45* (May 27, 1999). See also Dissenting Statement of Commissioner Harold Furchtgott-Roth (August 5, 1999). The FCC has gone to great lengths to ensure that the charges associated with the e-rate are not seen by the public as taxes. [See, for example, *In re: First report and Order and Further Notice of Proposed Rule-making, Truth-in-Billing and Billing Format; CC Docket 98-170* (May 11, 1999). In this "truth in billing" proceeding, the FCC effectively prohibited long distance carriers which pay into the fund from including on their bills a line showing the portion being passed through to consumers.] All documents available at [www.fcc.gov](http://www.fcc.gov).

long distance carriers to individual customers, increasing monthly bills by just over \$1 per month per line.<sup>7</sup>

The third major Federal tax levied on telecommunications services is the most ambiguous and controversial of all: It is the system of access charges imposed on long-distance carriers to compensate local carriers for use of the local facilities used to complete long distance calls. While a comprehensive analysis of the access charge system is far outside the scope of this paper, it is generally agreed that the charges are higher than can be justified by the economics of local access *per se*, and in fact are part of the “universal service” regime that holds prices for some customers below cost by raising prices on other customers. To the extent access charges represent *de facto* government mandated transfers from some customers to others, it is difficult to argue that they are not “taxes.”

*State and Local Taxes:* While Federal taxes on telecommunications services are both high and complex, state and local taxes are both much larger and far more complex.

As shown in Table Two below, there are approximately 37 different types of taxes levied on telecommunications services by state and local governments in the United States. These include excise taxes, franchise fees, right of way charges, gross receipts taxes, license fees, 911 fees, public utility taxes and even special levies for programs such as poison control centers. In some cases these taxes apply to local telephone services only; in others they extend across state borders and apply to long distance services as well. Wireless services are often taxed differently from landline services, and—as discussed further below—telecommunications services offered by non-traditional carriers such as competitive local exchange carriers (CLECS) may in practice be taxed differently from the same services when offered by traditional carriers.

Table Two:  
State and Local Telecommunications Taxes

State	Local/Municipal
Franchise Taxes .....	Franchise Taxes
Sales & Use Taxes .....	Sales & Use Taxes
Telecommunications Excise Taxes .....	Local 911 Tax
Gross Receipts Taxes .....	Excise Taxes
License Fees .....	Telecommunications Taxes
Utility Taxes, Utility User Taxes, PUC Fees .....	Gross Receipts Taxes
Rental/Lease Taxes .....	License Fees
Utility Sales Taxes .....	Utility Taxes
Business & Occupation Taxes .....	Access Line Tax
Infrastructure Maintenance Fees .....	Rental/Lease Taxes
911 Fees, Emergency Operation Charges, 911 Database Charges, 911 Equalization Surcharge.	Telephone Relay Surcharge/Universal Lifeline Surcharge
Intrastate Surcharge .....	Public Service Taxes
High Cost Fund Surcharge .....	Utility Users Tax
Relay Service, Communications Devices Surcharges, Universal Access Charges.	Infrastructure Maintenance Fees
Access Line Charges .....	Right-of-Way Charges
Infrastructure Fund Reimbursement .....	911 Fees
Poison Control Surcharge (TX) .....	Business & Occupation Taxes
Public Utility Commission Fees .....	
Teleconnect Fund .....	
Universal Service Charges, Universal Lifeline Telecommunications Surcharge	

Source: AT&T, The Progress & Freedom Foundation

One important data base for analysis of telecommunications taxes is contained in a survey published annually by the Federal Communications Commission. The FCC survey reports on 21 types of actual taxes, fees and other charges appearing on local telephone bills for 95 communities in 41 states.

The FCC data do not include taxes levied on long distance services, nor do they distinguish between taxes levied by state governments and those levied at the local level. However, they do make it possible to determine the overall level of Federal, state and local taxes on local phone bills in both absolute and percentage terms.

<sup>7</sup>The e-rate program has been roundly criticized by academic economists. See, for example, Jerry Hausman, *Taxation by Telecommunications Regulation: The Economics of the E-Rate*, (Washington: The AEI Press, 1998).

Table Three below summarizes this FCC survey data for the 20 highest-tax major metropolitan areas for 1997, the last year for which the Commission has made available the disaggregated data required for our purposes.<sup>8</sup> It shows that taxes on local telephone service amount to as much as 35 percent of the total phone bill, accounting in some jurisdictions for over \$4 per month, or as much as nearly \$60 per year. For the 95 jurisdictions overall, taxes average just over \$2 per month, or about 16 percent of the total local service bill.<sup>9</sup>

The FCC data also permit us to compare the relative magnitude of different types of taxes. As shown in Figure One (on the following page), state and local excise taxes account for over half (52 percent) of the taxes on a local telephone bill. State and local fixed fees add another four percent of the total, while 911 fees (also levied by state and local governments) make up yet another 22 percent. The Federal excise tax accounts for less than one fourth (22 percent) of the taxes on a local phone bill.

Table Three  
Telecommunications Taxes in the Twenty Highest-Tax Cities <sup>10</sup>

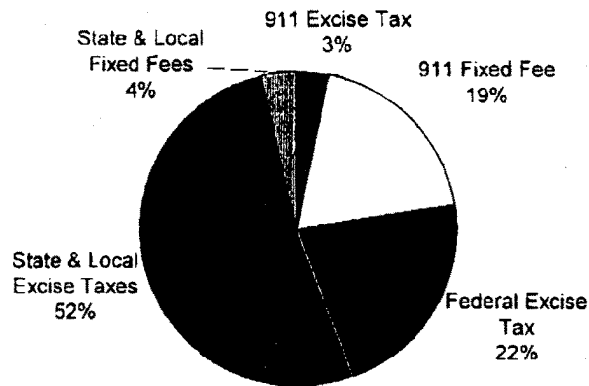
City	Tax	
	Amount	Rate
Richmond, VA .....	\$4.85	35.7%
Corpus Christi, TX .....	\$2.57	27.7%
Tampa, FL .....	\$3.06	25.9%
Chicago, IL .....	\$2.74	25.3%
Baltimore, MD .....	\$4.15	25.1%
Dallas, TX .....	\$2.63	24.9%
St. Louis, MO .....	\$2.57	22.7%
Kansas City, MO .....	\$2.55	22.5%
Brownsville, TX .....	\$1.99	22.2%
Houston, TX .....	\$2.44	21.7%
Los Angeles, CA .....	\$2.43	21.6%
San Antonio, TX .....	\$2.10	21.0%
Fort Worth, TX .....	\$1.93	19.2%
Oakland, CA .....	\$2.14	19.0%
Atlanta, GA .....	\$3.31	19.0%
Salinas, CA .....	\$1.97	17.5%
San Jose, CA .....	\$1.85	16.5%
Miami, FL .....	\$1.73	16.2%
Detroit, MI .....	\$2.15	16.2%
Huntsville, AL .....	\$2.48	15.2%
<b>Weighted Average (95 Cities) .....</b>	<b>\$2.04</b>	<b>15.7%</b>

<sup>10</sup> Calculated based on data collected by the Federal Communications Commission. Listed cities include only those over 100,000 population. Weighted average includes all 95 cities in sample. Taxes include the Federal excise tax (3%), state and local excise taxes, state and local fixed taxes, 911 excise taxes and 911 fixed taxes appearing on local residential telephone bills. Additional taxes (e.g. franchise taxes, public utility taxes, property taxes, etc.) not shown on the customer's bill are not included, nor is the Federal Subscriber Line Charge. See **1999 Reference Book of Rates, Price Indices, and Expenditures for Telephone Service** (Industry Analysis Division, Common Carrier Bureau, Federal Communications Commission, February 1999), Table 14.1. The disaggregated data used to calculate the figures in this table are posted on the FCC's Web site, at [www.fcc.gov/Bureaus/Common-Carrier/Reports/FCC-State-Link/lec.html](http://www.fcc.gov/Bureaus/Common-Carrier/Reports/FCC-State-Link/lec.html)

<sup>8</sup> While data from its 1990-1997 surveys is posted on the FCC's Web site, Commission staff have refused without explanation repeated requests to make available the 1998 data needed to break out the various components of taxes and fees that make up local bills. We remain hopeful this data will be made available in the immediate future.

<sup>9</sup> These figures are broadly consistent with those reported in the COST study, which found an overall average rate of 18 percent nationally, with the highest state-average rate approaching 30 percent.

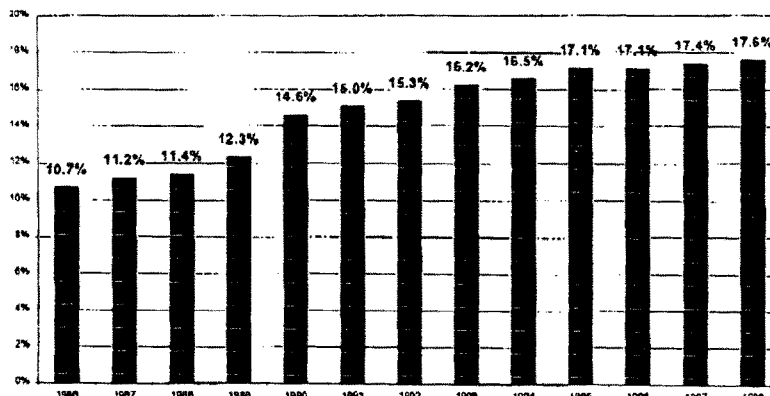
Figure 1: Composition of Telecom Taxes



Because these figures include only taxes that are imposed on local telephone service, they do not reflect the Federal "e-rate" tax (which is imposed on long-distance carriers and passed through to consumers on long-distance bills). Similarly, they do not account for the portion of the Federal excise tax applied to long distance charges, or whatever portion of Federally mandated access charges one might attribute to universal service and thus appropriately characterize as a tax. Even if these charges were included, however, they would not change the basic conclusion that emerges from Figure One: On average, states and localities tax telecommunications even more heavily than does the Federal government.<sup>11</sup>

The FCC data also permit an examination of the trend in telecommunications taxes over time. As shown in Figure Two below, the trend is towards significantly higher taxes. Since 1986, the average tax rate on local phone bills has risen from 10.7 percent to 17.6 percent. In dollar terms, taxes on the average monthly phone bill have risen by 62 percent during this period, from \$1.51 in 1986 to \$2.41 in 1998.

Figure 2: Telecommunications Tax Rates 1986-1998



Source: Federal Communications Commission, Trends in Telephone Service (February 1999), Table 14.1.<sup>12</sup>

In summary, telecommunications taxes in the United States are numerous, complex, and high relative to other goods and services—and getting higher.

<sup>11</sup> Again, this conclusion is consistent with the findings of the COST study.

<sup>12</sup> The PFF estimates in Table Three above are based on a somewhat more conservative methodology than that used by the FCC to calculate the percentages in Figure Two above. Thus, the FCC estimates the average tax rate in 1997 as 17.4 percent, compared with PFF's 15.7 percent.



*The High Cost of Taxing Telecom*

Economists and other policy analysts agree on three broad criteria by which tax policy should be judged: Efficiency, equity and enforceability. The efficiency criteria implies that taxes should reduce overall economic welfare as little as possible. The equity criteria suggests that taxes should contribute to (or at least not detract from) some generally accepted sense of fairness in the distribution of income and wealth. The enforceability criteria simply means that taxes ought to be designed in a way that minimizes the administrative and other costs of collecting them.

In the pre-competition, pre-Internet world of plain old telephone service, telecommunications taxes probably looked relatively good by these traditional standards of tax analysis:

- *Efficiency*: Historically, telecommunications taxes probably caused relatively small welfare losses. This is because the quantity of plain old telephone service (POTS) purchased (especially local service) was relatively insensitive to price (it was *price inelastic*), and thus unresponsive to any price increases caused by high tax rates.<sup>13</sup> So long as taxes did not produce large changes in the quantity or types of telecommunications services purchased, the misallocation of economic resources caused by telecommunications taxes was small.
- *Equity*: Telecommunications taxes were part and parcel of a system of price regulation that provided significant subsidies for those at the lower end of the income spectrum or who, for whatever reason, were felt to deserve relatively low telephone prices. And, because telecommunications carriers were guaranteed a regulatory rate of return, neither they nor their shareholders suffered when taxes were raised.
- *Enforceability*: Telecommunications taxes were levied on a single provider, the monopoly telephone company, which was sufficiently large and sophisticated to comply efficiently with even a fairly complex tax regime. To the extent there were ambiguities in the system, these could be worked out between the lawyers for the phone company and the tax collectors, probably in conjunction with the state regulators.

As discussed in the Appendix, however, there are massive changes underway in the telecommunications marketplace. These changes turn the calculus of telecommunications taxes on its head. Whereas telecommunications taxes may once have been relatively desirable (as compared with other taxes), they are now arguably the most destructive taxes being levied on the American economy.

The work now underway at The Progress & Freedom Foundation aims to present a complete analysis of the impact of telecommunications taxes, and the objective of this paper is not to anticipate or prejudge the results of that analysis. At the same time, it is already quite apparent that, in today's converged, digital, Internet-defined marketplace, telecommunications taxes do not hold up well to the scrutiny of the traditional analysis described above.

*Telecom Taxes and Economic Efficiency*: From the perspective of tax analysis, the most significant change in telecommunications markets may lie in the changing nature of telecommunications demand. Whereas demand for POTS was relatively inelastic, demand for the vast array of new telecommunications products appears to be relatively price elastic. Technically, this means that a relatively small percentage change in the price of telecommunications products results in a relatively large percentage change in the quantity purchased. In practical terms, it means that telecommunications taxes may cause many people to purchase fewer telecommunications services than economic efficiency would require.

Consider, perhaps most importantly, the market for broadband communications—i.e. for high-speed connections to the Internet. In the past, high-speed Internet access was available only through so-called “T-1” lines which, at \$2,000 or more per month, were affordable only by large corporations or the very wealthy. Recently, however, two new technologies have emerged that make broadband access potentially affordable for virtually everyone. Digital Subscriber Line (or “DSL”) technology allows a standard telephone line to be converted into a high-speed data line. Offered by the major telephone companies, as well as a growing cadre of competitive “CLECs” and “DLECs,” DSL services are being offered in many areas of the country for \$40-\$60 per month. At the same time, Cable Modem technology is now offering very similar services at competitive prices.<sup>14</sup>

<sup>13</sup>The demand for basic local telephone service is highly inelastic. See, for example, Hausman, 1999.

<sup>14</sup>See Federal Communications Commission, *Inquiry Concerning the Deployment of Advanced Telecommunications Capability* (CC Docket 98-146, August 7, 1998).

Making affordable broadband services available to all Americans is one of America's highest economic priorities. As FCC Chairman Bill Kennard put it in a recent speech, "despite all the technical advances and globalization, the formula for economic success has remained the same: economic prosperity relies on high-speed access to the critical network of information and commerce. That network is the Internet, and the type of access needed is broadband."<sup>15</sup>

The available evidence suggests that demand for broadband services is highly elastic—that is, sensitive to price. A recent study by Robert Crandall and Chuck Jackson, for example, estimated that only four million consumers would be willing to pay \$70 per month for an upgrade from 56.6 kb/s Internet access to 1.1 Mb/s, but 20 million would pay \$25.<sup>16</sup>

Applying the available evidence on elasticities of demand for broadband services to current telecommunications tax rates yields disturbing results. Indeed, as shown in Table Four below, the available evidence suggests telecommunications taxes already are having a significant impact in slowing the adoption of high speed Internet access to American households. And, as the number of households with access to broadband services grows, this effect will grow in the future. Specifically, at the national average telecom tax rate of 16 percent, we estimate that at least 165,000 households, and perhaps as many as 2.9 million households, are being effectively priced out of the market for broadband Internet access in 1999. As the availability of broadband services spreads, and the number of potential customers grows, these estimates go up significantly over time. By 2002, at current tax rates, we estimate that between 1.2 million and 4.2 million households will be denied broadband Internet access by high telecommunications taxes.

If telecommunications taxes were to continue to rise, the impact would grow more than proportionately. For example, a 20 percent tax burden (similar to current rates in Baltimore, Dallas, Los Angeles and Tampa) is estimated to reduce broadband penetration by approximately 11 percent. However, a 33 percent burden (similar to the current rate in Richmond, Virginia) reduces predicted broadband penetration by nearly 20 percent.

Table Four:  
The Impact of Telecommunications Taxes on Broadband Penetration

Tax Rate <sup>17</sup>	Impact on Penetration (Percent) <sup>18</sup>	Households Denied Internet Access <sup>19</sup>	Children in Households Denied Internet Access <sup>20</sup>
<b>1999</b>			
16% .....	-7.5% .....	0.2 million-2.9 million ....	0.1 million-1.9 million
20% .....	-9.3% .....	0.2 million-3.6 million ....	0.1 million-2.3 million
33% .....	-18.9% .....	0.4 million-7.3 million ....	0.3 million-4.8 million
<b>2002</b>			
16% .....	-7.5% .....	1.2 million-4.2 million ....	0.8 million-2.7 million
20% .....	-9.3% .....	1.5 million-5.2 million ....	1.0 million-3.4 million
33% .....	-18.9% .....	3.0 million-10.6 million ..	1.9 million-6.9 million

Source: The Progress & Freedom Foundation

<sup>17</sup> Actual tax rate applied to sales of broadband services, per month per line, irrespective of whether applied on a percentage or per line basis.

<sup>18</sup> Arc price elasticities of demand are assumed to be -0.51 in the \$40-\$50 range and -1.23 in the \$50-\$60 range. See Crandall & Jackson, p. 26. Costs are assumed to be constant at \$40 throughout the range of output.

<sup>19</sup> Upper bound based on estimate of 38.8 million Internet connected households in 1999; 56.0 million Internet connected households in 2002. Lower bound based on estimate of 2.2 million broadband-connected households in 1999; 15.8 million broadband connected households in 2002. Both estimates by Forrester Research. See Erran Carmel, Jeffrey A. Eisenach and Thomas M. Lenard. *The Digital Economy Fact Book* (Washington: The Progress & Freedom Foundation, 1999), pp. 7, 35. Hereafter cited as Fact Book.

<sup>20</sup> Based on U.S. Census Bureau, *Current Population Reports*, March 1998 Update (Approximately 35 percent of American households have children under 18 living at home, and these families have an average of 1.86 children per family).

**Telecom Taxes and Equity:** The equity consequences of telecommunications taxes are also being affected by the changing marketplace. As noted above, telecommunications taxes in the pre-competition, pre-digital environment were part and parcel of a regulatory regime that set virtually all prices at levels designed to ensure equity while offering a fair return to telephone companies. Thus, prices could be set in such a way as to offset the inherently regressive nature of fixed and excise (i.e. percentage) taxes on telecommunications.

<sup>15</sup> Hon. William Kennard, "The Road Not Taken: Building a Broadband Future for America," Speech to the National Cable Television Association, June 16, 1999.

<sup>16</sup> See Robert W. Crandall and Charles L. Jackson, *Eliminating Barriers to DSL Service*, unpublished manuscript, May 1998.

In a competitive environment, of course, such cross-subsidies are simply unsustainable, and indeed the Federal Communications Commission is moving gradually in the direction of reducing and/or eliminating such cross subsidies.

For products, like POTS, where elasticities of demand are low and prices (even if allowed to rise to full cost) are affordable for most families, the impact of removing such cross subsidies should be relatively small. Again, however, the analysis is quite different when one considers the full impact of telecommunications taxes on products with high elasticities of demand.

Returning again to the example in Table Four above, we have estimated the impact of current and possible future telecommunications taxes on the availability of at-home broadband Internet access for children. As shown in the table, we estimate that, at current tax rates, between 800,000 and 2.7 million children will be denied such access over the next three years.

It should also be noted that these figures reflect the average impact of telecommunications taxes on all customers, assuming all are equally sensitive to price changes. This assumption is open to question, in at least two specific ways. First, households with lower incomes are likely to be more sensitive to changes in telecommunications prices than those with higher incomes.<sup>21</sup> Thus, telecommunications taxes are likely to deny broadband access to proportionately more “poor” families (and their children) than to the rich. Second, because the costs of deploying broadband services in rural areas are higher and rural incomes are lower than the national average, it is also likely that high telecommunications taxes will have a greater impact on rural areas than on urban or suburban ones. Thus, telecommunications taxes contribute directly to the digital divide, whether it is expressed in terms of geography, income or both.

*Telecom Taxes and Enforceability:* As discussed further in the Appendix, the emerging market for telecommunications services is the antithesis of a monopoly. As former White House Internet Advisor Ira Magaziner put it in a recent Progress & Freedom Foundation paper, “with the Internet and this new environment of convergence, we are going to have the greatest amount of competition the world has ever seen.”

The competition now breaking out in the telecommunications marketplace is of two types. First, it consists of numerous companies all competing to offer the same product in the same market. Thus, nearly all U.S. markets now have more than one company offering local telephone service, and most states have literally dozens of companies—many of them small and relatively young—offering telephone services in their states. An obvious implication of this sort of competition for telecommunications taxes is to increase administrative costs for both tax collectors and for the companies. And, because such costs are, in effect, fixed costs of entering new markets, they end up serving as barriers to entry, thereby reducing economic efficiency.

The second type of competition is even more problematic for tax authorities: It is competition to offer new and different services, often through new and different means. It is here that the current tax regime begins simply to collapse.

When, for example, is a service a “telecommunications service”? This used to be a pretty straightforward question: It was a telecommunications service if it was offered by the phone company. Then along came wireless (i.e. cellular) telephony. For the most part, wireless telephony was also treated as a telecommunications service. At about this same time, AT&T was broken up into its local and long-distance components. Could the states tax the long distance (interstate) part of the bill? As it turned out, under a 1989 Supreme Court decision, they could: Interstate calls were telecommunications services too.

Once data services are added to the pot, however, the question becomes far more ambiguous. Is “Internet access” a telecommunications service? The answer, at the moment, is that no one knows for sure. Indeed, just two weeks ago, on August 25, 1999, the U.S. Court of Appeals for the District of Columbia granted the FCC’s request to remand an August 1998 order determining that “advanced” telecommunications services are either “telephone exchange” or “telephone access” services.<sup>22</sup> In other words, even the national authority on telecommunications policy—the FCC—isn’t sure what counts as telecommunications anymore.

In fact, the question of who should pay telecommunications taxes, and on what tax base, is certain to get more complex before it gets simpler. For example:<sup>23</sup>

<sup>21</sup> See, for example, U.S. Department of Commerce, *Falling Through the Net* (July 1999), p. 81.

<sup>22</sup> See Federal Communications Commission, “Comments Requested in Connection with Court Remand of August 1998 Advanced Services Order” (Public Notice, September 9, 1999).

<sup>23</sup> The issues described below are illustrative of a vast array of questions now facing taxing authorities with respect to telecommunications taxes. For one thoughtful review of such issues,

- When telephone companies bundle Internet Service Provider services with DSL services, are those services taxable as telecommunications services? Or are they exempt from taxation under the moratorium imposed by the Internet Tax Freedom Act? Perhaps they are taxable only in part. If so, how should taxing authorities decide where to draw the line?
- Does the answer to the above question change if the same service is provided by an Internet Service Provider using DSL lines leased from a telephone company? (The answer, apparently, is that it depends what state you are in, as some states in fact treat the two situations differently while others treat them the same.)
- Is broadband Internet access offered by a cable television company a telecommunications service? What if the service is offered over telephone lines leased from a phone company? If it is offered over the cable company's own phone lines?

The list of such questions could go on indefinitely—and, on the current path, it will, as each of these questions and literally thousands more will need to be decided by taxing authorities all across the U.S. It seems unlikely that the decisions they reach will be consistent with one another, forcing telecommunications providers to create increasingly complex compliance systems—or, again, to choose not to enter some markets in order to avoid the administrative burdens of doing so.

In summary, applying the current, highly complex system of telecommunications taxes to the new, competitive telecommunications market will create serious problems of enforceability, imposing high compliance costs on both tax collectors and companies.

#### *Conclusions and Tentative Policy Implications*

The circumstances that made it possible to subject telecommunications services to a complex system of extremely high tax rates have changed. In fact, the same traditional tax policy analysis that suggests that telecommunications taxes were relatively efficient ways to raise revenue in the pre-competition, pre-Internet environment strongly suggests that they are quite costly and highly inefficient today.

Policymakers need to re-examine the panoply of taxes currently applied to telecommunications with an eye towards both tax simplification and tax reduction. For states and localities, which together account for more than three-fourths of all telecom taxes, there is an urgent need to put such reforms in place at a pace consistent with the rapid development of the marketplace. In this case, at least, tax policy needs to be worked on “on Internet time.”

#### APPENDIX:

##### THE CHANGING MARKET FOR TELECOMMUNICATIONS

The market for telecommunications has changed dramatically in recent years. It has changed from a natural monopoly to a competitive market. It has changed from technologically homogenous and stable market to one with many competing and rapidly changing technologies. And, it has changed from a market that followed the overall economy to one that is, more than any other, leading it.

For most of its history, the telecommunications industry has been thought of as a natural monopoly and regulated as a traditional public utility. During the 1970s and 1980s, however, technological progress began to transform the telecommunications marketplace into one in which competition was both possible and desirable. In the 1980s, digital switching technologies first made it economical to interconnect multiple long distance and wireless carriers to the local switching system. The results were the breakup of AT&T, the creation of the cellular telephone industry and the development of competitive markets for both long distance and wireless telephone services. Local telephone service, however, continued to be viewed as a natural monopoly and regulated as a public utility.

By 1996, it was generally agreed that further technological progress was rapidly making competition possible not only in the long distance and wireless markets, but also in the market for local telephone service. Similarly, most policymakers agreed that, thanks largely to competition from direct satellite broadcasting, the market for cable television was also becoming competitive. Recognizing these changes, Congress passed Telecommunications Act of 1996, which ended rate regulation of cable television and initiated a transition to a competitive market for local telephone service.

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see Richard McHugh, *Sales Taxation of Telecommunications Service in the State of Utah* (Georgia State University School of Policy Studies, February 1997).

Importantly, the Telecommunications Act also called for an end to the use of hidden cross subsidies, concealed within regulated prices, that previously had kept some prices (e.g. rates for basic telephone services in rural areas) below cost while artificially raising others (e.g. rates for urban business customers). As Congress correctly recognized, a precondition for competition was that prices reflect the actual costs of providing services, and thus that any cross-subsidies be made explicit.

One phenomenon the Telecommunications Act could not and did not anticipate was the explosive growth of the Internet and its impact on the telecommunications network.<sup>24</sup> The Internet has resulted in very rapid growth in the volume of data travelling on the public switched telephone network, to the point that data traffic will soon exceed voice traffic. The resulting demand for data transport (especially for the high-capacity broadband transport needed to facilitate increasingly rich Internet-based applications and to support electronic commerce), combined with the competitive framework established by the Telecommunications Act, has led to an explosive growth in the number and the types of both telecommunications services and telecommunications providers.

The impact of these changes on the nature of the telecommunications marketplace is quite profound. As former White House Internet advisor Ira Magaziner explains in a recent Progress & Freedom Foundation publication:

With the Internet and this new environment of convergence, we are going to have the greatest amount of competition the world has ever seen. We are going to have telecom companies, computer companies, software companies, satellite companies, wireless companies, consumer electronics companies, and electric utilities all competing to build out this infrastructure, and the best thing we could do is let that competition take place and not try to regulate it or interfere with it.<sup>25</sup>

As Magaziner explains, technological convergence has brought previously separate sectors of the telecommunications industry into direct competition with one another. Most notably, the cable industry has become a major competitor in the market for telecommunications services of all kinds, especially broadband communications offered through cable modems.<sup>26</sup>

These changes are no longer a matter of speculation. Indeed, in the first paragraph of its recently released restructuring proposal, the Federal Communications Commission states unequivocally that:

In five years, we expect U.S. communications markets to be characterized predominantly by vigorous competition that will greatly reduce the need for direct regulation. The advent of Internet-based and other new technology-driven communication services will continue to erode the traditional regulatory distinctions between different sectors of the communications industry.<sup>27</sup>

The third major change—and the one that makes reform of telecommunications taxes so crucially important—is that the telecommunications sector has become the catalyst for overall macroeconomic growth. Indeed, most economists now agree that the information technology sector of the economy is responsible for a disproportionate share of American economic growth in recent years.

Testifying before Congress in February 1998, for example, Federal Reserve Board Chairman Alan Greenspan stated that:

[O]ur nation has been experiencing a higher growth rate of productivity—output per hour worked—in recent years. The dramatic improvements in computing power and communications and information technology appear to have been a major force behind this beneficial trend.<sup>28</sup>

More recently, the U.S. Department of Commerce has reported that the information technology sector of the economy (which includes telecommunications)—though making up less than 10 percent of total output and employment—is responsible for over 40 percent of growth in Gross Domestic Product.<sup>29</sup>

These statistics highlight the importance of constructing a sensible public policy framework that permits and encourages continued growth in the telecommuni-

<sup>24</sup> While growth of the Internet has slowed somewhat since 1995, it continues to grow by 50 percent or more per year, as measured by the number of Internet host computers (and faster by some other measures). See Erran Carmel, Jeffrey A. Eisenach and Thomas M. Lenard, *The Digital Economy Fact Book* (Washington: The Progress & Freedom Foundation, 1999).

<sup>25</sup> See Ira Magaziner, "Creating a Framework for Global Electronic Commerce," *Future Insight* 6.1, (Washington: The Progress & Freedom Foundation, July 1999).

<sup>26</sup> See Barbara Esbin, *Internet Over Cable: Defining the Future in Terms of the Past* (Office of Plans and Policy, Federal Communications Commission) OPP Working Paper No. 30, August 1998. See also

<sup>27</sup> A New FCC for the 21st Century (Federal Communications Commission, August 1999)

<sup>28</sup> Alan Greenspan, Monetary Policy Testimony and Report to Congress, February 24, 1998.

<sup>29</sup> See U.S. Department of Commerce, *The Emerging Digital Economy II* (June 1999).

cations sector. Obviously, tax policy is an important part of any such framework. As discussed in the body of this paper, our current policies are a long way from meeting this standard.

Mr. TAUZIN. And just for a couple of minutes to highlight some of his findings, extraordinary findings. First of all, the combination of State, Federal, and local taxes since 1986 on telecommunications services has risen from 10.7 percent now to 17.6 percent. The taxes in many jurisdictions of State, Federal, and local on telephone talking in America, free speech society are now higher than the taxes on such so-called sin products as alcohol and tobacco.

It points out that there are approximately 37 different types of taxes levied on telecommunications services by State and local governments alone and that for some cities, for example, Richmond, Virginia, the rate of local taxation and city taxation, State taxation, now 35.7 percent of the telecommunications services. 35.7 percent State and local only, then you add all of these Federal taxes on top of it.

In short, the study indicates that if there is one thing that makes it harder for us to provide telecommunications services to the poorest of Americans, it is because the government takes out of those services from the get-go in the form of taxation. And I think it strongly supports the effort that we are jointly making to reduce taxes on telecommunications services and at the same time use some of those taxes, one-third of the 1913, 3 percent telephone tax, to continue and to hopefully make better a program out of Internet connection for our children.

So, gentlemen, I want to thank you for your contributions and I know the leg work that you are doing to try to encourage other members to pay attention to this one because it is not only a constitutional problem, Mr. Weller, as you point out, for the Ways and Means Committee and the Congress, but it is as many of our witnesses will later tell us, an administration problem, a policy question. Do we let the FCC run this education program? Or do we let the educators with the guidance and advice of our National Telecommunications Agency here in Washington that tends to follow all the new technologies and probably can recommend a wireless technology, perhaps over a wire technology, that may have a better utility for the kids in the future.

In Baton Rouge on October 11 I will be having a major high-tech conference. We will introduce there technology that will put kids on the Internet for \$5 a month on television. Analog television. Not digital. Today, \$5 a month. And we will probably be announcing some pilot programs to make it available free to eighth graders in several school districts as a pilot program in their homes just to test it out and see the power of connecting kids to the Internet without the necessity of many of the expenditures this program entails.

And so, again I want to thank you and ask if any of our colleagues have any questions or comments they would like to make while you are here and to engage you in any kind of colloquy. Mr. Markey? Any one of you?

Mr. MARKEY. I thank you so much. This is a very complex policy area because obviously a huge decision was made back in the

1930's to create a universal service structure, so that people from Boston would subsidize people in rural America.

Mr. TAUZIN. And we appreciate it.

Mr. MARKEY. I appreciate that. But the question I would have to our witnesses is whether or not they would support a line item that would explain to each ratepayer how much higher their phone bill is in Boston because they are subsidizing rural America. And would they also put a line item on—support a line item for rural America so they would understand how much lower their bill is that it would be a doubling or tripling or quadrupling of their phone bill if we pull out those taxes—using the terminology that the majority is using. They consider this taxes—that goes in urban America to help out rural America. Would you support having that as a line item as well?

Mr. WELLER. Mr. Markey, I find I represent South Side of Chicago and the suburbs. I have the neighboring district to my friend Mr. Rush as well as a lot of rural areas and I think that the rural areas feel they are subsidizing the folks in the cities on various issues and so forth.

Mr. MARKEY. But I just mean in this area of universal service where there is a phone bill which is used here to subsidize ensuring that the schools of the poorest communities especially but all schools qualify, but the poor schools get this additional funding to hook up, we do the same thing for farmers. My father was a milkman for the Hood Milk Company and his phone bill subsidizes wealthy farmers. And should he know that in—should every American know that the poor city—not the poor, but the working class city dwellers are subsidizing rural America and it is right on their phone bill and each year they are paying all of this extra money so the rural farmer can have a lower phone bill? Should that be on each, as a line item on each phone bill?

Mr. WELLER. It sounds like it could be a subject of a potential future hearing but the challenge before us today is really what type of tax do we use to fund a program which has bipartisan support and that is providing Internet access through our local schools and libraries? And I certainly believe as a member of the Ways and Means Committee that under our Constitution it is Congress' job to levy a tax. And of course the issue before us is the case where the FCC levied a tax without the approval of Congress.

And while we all support Internet access through our local libraries and schools and that is a goal we all share, the question is how best can we fund it? And we believe that with our legislation, the Schools and Libraries Internet Access Act, the most appropriate thing to do is to earmark an existing tax that has been in place since 1913, one penny on the dollar will provide—one-third of that existing tax will provide \$1.7 billion, which is actually more than the existing FCC tax. And perhaps it should be labeled "the FCC tax on the phone bill" so that people identify who gave it to them and why it is unconstitutional.

Mr. MARKEY. I guess the only point I am trying to make here is that it would be honest for these subsidies to be on your bill so that there is just a line saying you are subsidizing schools and libraries, you are subsidizing rural Americans and then everyone would know it. It would cause a huge furor, of course, in urban America

if we ever put that on as a line item. Phone bills are three or four times lower in rural America than they should be just because of some policy was made of universal service but just truth in billing and the honesty of ensuring that people understand the level of subsidies that do flow through this universal service fund not just to poor children but also to wealthy farmers, I think would help to have a good honest debate on this.

Mr. TANCREDO. I couldn't disagree with you. I think it would be fine. I recognize fully well the interesting political ramifications that may develop out of such honesty on a phone bill and on a tax policy. But that is exactly why we are here. And I am suggesting that what we are doing today is dishonest. I am suggesting that we should be much more forthcoming with the gentleman from my district and everybody else who receives a phone bill and is trying to figure out exactly what all of these taxes are paying for. And I would be more than willing to explain that directly.

And you know, the fact is that there is a great degree of cynicism, and we all know that, on the part of the general public. Tax policies such as the ones that we are here today to try to address I think only tend to exacerbate that cynicism that exists on the part of the American public. And a degree of candor that you suggest might go a long way toward reducing that. So I have no qualms about that.

Mr. MARKEY. Can you go along with that, Jerry? To list on—

Mrs. WILSON. Will the gentleman yield? Does he have a list of those wealthy farmers because I am not sure I have met any.

Mr. MARKEY. I am listening to my father speak. That was his view of it.

Mrs. WILSON. That is a certain downtown Boston prejudice.

Mr. WELLER. In quick response, Mr. Markey and Mr. Chairman, as Chairman Tauzin pointed out, roughly 35 percent of the cost of telecommunications today is consumed by taxes imposed at the local and State level. And then, of course this is an additional tax imposed at the Federal level. And, of course, then the 3 percent excise tax that was imposed beginning 1913. I think it is very helpful that the American people have an understanding of the high level of tax burden that has been placed on them. When 40 percent of the average Illinois family's income is going to government today, that tax burden is too high, when 21 percent of our gross domestic product is consumed by the Federal Government. In 1993 it was only about 18 percent. So that tax burden is so high and I think it is useful that we share with the American people every opportunity that we identify how high that tax burden is.

Mr. MARKEY. So you would support this as a line item, Jerry?

Mr. WELLER. It is something that you and I could talk about some more.

Mr. MARKEY. Let's have some principles here, Jerry. Principles.

Mr. WELLER. It is a useful discussion.

Mr. TAUZIN. I think we need to get your dad in on that meeting. We have to break for a vote and come back and hear the next panel. We thank both of you. It has been a very exciting and useful discussion. Come back after the vote.

[Brief recess.]



Mr. TAUZIN. The committee will please come back to order and our guests will take seats. We are pleased to welcome our second panel, composed of Mr. Christopher Wright, General Counsel of the FCC; Mrs. Kelly Levy, Acting Associate Administrator, Office of Policy Analysis and Development for the National Telecommunications and Information Administration; Dr. Lois Gerber, Chairman of the board of National Independent Private Schools Association; Cheryl Parrino, CEO of the Universal Service Administrative Company; and Mr. Kent Lassman, Deputy Director of Technology and Communications for the Citizens for Sound Economy.

Ladies and gentlemen, thank you for your attendance today. We welcome your testimony. We have a 5-minute rule. And we have this incredible marvelous modern technology that we use to time you, along with eggs, which we cook in the back room. So when the bell goes off, your 5 minutes is up. We would like you to know that your written statement is part of the record. You don't have to read them to us. Please don't. Give us the highlights in the 5 minutes that you have so that we can get into a Q and A with you as rapidly as possible.

We will start with Mr. Christopher Wright of the FCC.

**STATEMENTS OF CHRISTOPHER J. WRIGHT, GENERAL COUNSEL, FEDERAL COMMUNICATIONS COMMISSION; KELLY KLEGAR LEVY, ACTING ASSOCIATE ADMINISTRATOR, OFFICE OF POLICY ANALYSIS AND DEVELOPMENT, NATIONAL TELECOMMUNICATIONS AND INFORMATION ADMINISTRATION, U.S. DEPARTMENT OF COMMERCE; LOIS M. GERBER, CHAIRMAN OF THE BOARD, NATIONAL INDEPENDENT PRIVATE SCHOOLS ASSOCIATION; CHERYL PARRINO, CEO, UNIVERSAL SERVICE ADMINISTRATIVE COMPANY; AND KENT LASSMAN, DEPUTY DIRECTOR, TECHNOLOGY AND COMMUNICATIONS, CITIZENS FOR A SOUND ECONOMY**

Mr. WRIGHT. Thank you, Chairman Tauzin. Last December 1 I had the wonderful opportunity to visit New Orleans for only the second time in my life and argue the case in the Fifth Circuit, and there were 10 attacks on the schools and libraries program and we won nine.

Mr. TAUZIN. Which one did you lose?

Mr. WRIGHT. The jurisdictional argument. Cincinnati Bell claimed that the way that we assessed the amounts was incorrect, that we should only assess based on interstate rather than intrastate revenues. It is a decision that is troubling to us, but has nothing to do with—it has to do with the relative amounts the different telephone companies pay rather than anything that is of interest to this committee.

The nine issues on which we prevailed were divided into two groups. There were four constitutional attacks, all made by Celpage, and there were five statutory attacks, all made by GTE. And we won all of the four constitutional attacks in short order. It was a great range of attacks. The telecom industry is extraordinarily resourceful and litigious. They claimed the program violated the origination clause, the taxing clause, the equal protection clause, and the takings clause. And in light of your admonition that

our testimony is in the record, I will not go through each one of those except to say that we won each and every one of those.

GTE's five statutory arguments were, first, that it was erroneous under the statute to fund internal connections and Internet access, an issue that the Court gave the most attention to and certainly found merit in GTE's position, although it ultimately held that the statute was ambiguous and the Commission's reading of it was proper and affirmed.

Mr. TAUZIN. In fact he did more. He called it sometimes mysterious section.

Mr. WRIGHT. That is what the Fifth Circuit said, not us.

But I take it that there is really no dispute anymore that internal connections and Internet access ought to be funded. As I understand it, your bill would do that in a different way.

The next issue that we won on that the Fifth Circuit gave some attention to was GTE's argument that only telephone companies like itself should get money out of the system. That if a school district wanted to obtain Internet access from a lower priced provider like AOL they couldn't choose them. The Fifth Circuit rejected that claim. GTE also argued that we funded too many telecommunications services. The Fifth Circuit rejected that claim. And rejected two other GTE claims that I don't really think warrant attention here.

So it took 3½ years to get where we are. We completed our rule-making on Congress' schedule 15 months after the act was passed. It took the Court of Appeals more than 2 years after that to reject these 9 out of 10 challenges. No one sought rehearing on any of these nine issues. And it is possible that someone could still raise some in the Supreme Court. But that would surprise me.

Mr. TAUZIN. If I could interrupt you, has there been an appeal or will there be an appeal to this ruling?

Mr. WRIGHT. Petitions for certiorari in the Supreme Court are not due until December. The parties haven't shared with me their plans but it took us 3½ years to get there. We view it as now being essentially settled, these key elements. The danger of disrupting the program that is in place is that the bill that is proposed would require the Department of Commerce to hold a rulemaking and I fear that would have the potential of setting up another round of litigation.

My former colleague and friend, Andy Pincus, who is General Counsel of the Department of Commerce, would, I guess, then take over on that. But if that litigation proceeds on the same schedule we would be in the year 2003 before we get the clarity we now have.

Thank you.

[The prepared statement of Christopher J. Wright follows:]

PREPARED STATEMENT OF CHRISTOPHER J. WRIGHT, GENERAL COUNSEL, FEDERAL COMMUNICATIONS COMMISSION

Mr. Chairman and Members of the Subcommittee: I am pleased to be here today representing the Federal Communications Commission to discuss H.R. 1746, the "Schools and Libraries Internet Access Act." The bill would repeal Section 254(h) of the Communications Act, which authorizes the Commission to provide support to schools and libraries for the purpose of purchasing telecommunications services, internal connections, and internet access. The bill would replace Section 254(h) with a new provision that directs the Secretary of Commerce to "prescribe such regula-

tions as may be necessary” to govern the distribution of funds to schools and libraries to purchase “telecommunications and related services” and the “installation of equipment...essential to permit such school or library to have access to advanced technologies.” H.R. 1746, § 5 (adding Section 106(a)(5) to the National Telecommunications and Information Administration Organization Act).

As general counsel for the Commission, I think it would be most helpful for me to focus on the relevant provisions of the universal service decision that the Fifth Circuit issued this past July. See *Texas Office of Public Utility Counsel v. FCC*, 183 F.3d 393 (5th Cir. 1999). That decision affirmed the key elements of the Commission’s implementation of Section 254(h), and thus puts to rest many of the legal questions that have been raised concerning the Commission’s schools and libraries program. The replacement of Section 254 with a similar provision could lead to delay and uncertainty because the Commerce Department would first have to issue rules implementing the new provision and then defend its interpretation in court. Although the Commission issued its order implementing Section 254(h) exactly 15 months after its enactment, as Congress directed, it took the court of appeals more than two years to resolve the legal challenges to the program raised by Celpage, GTE, and Cincinnati Bell. If H.R. 1746 were adopted tomorrow and a rulemaking and litigation followed on the same course, it would be 2003 before a court of appeals issued a ruling resolving the challenges that would almost inevitably follow.

#### *The Fifth Circuit Decision*

In most—but not all—respects, the Fifth Circuit upheld the Commission’s May 8, 1997, order implementing the universal service provisions of the Communications Act.

As relevant here, the court first rejected Celpage’s various arguments that the Commission’s schools and libraries program is an “unconstitutional tax” or is otherwise unconstitutional. By and large, the court dispatched these claims summarily. Celpage’s principal argument was that Section 254(h) is a “Bill for raising Revenue” within the meaning of the Origination Clause, U.S. Const., art. I, § 7, cl. 1, and hence unconstitutional because it originated in the Senate rather than the House of Representatives. The court held that Celpage’s “Origination Clause claim cannot survive *United States v. Munoz-Flores*, 495 U.S. 385, 398 (1990),...because ‘a statute that creates a particular government program and that raises revenue to support that program...is not a ‘Bil[l] for raising Revenue’ within the meaning of the Origination Clause.” 183 F.3d at 427. The court dismissed Celpage’s claim based on the Taxing Clause, U.S. Const. art. I, § 8, cl. 1, in a footnote. The court explained that, in light of the clear nexus between the payments made by telecommunications carriers under Section 254(d) and the program supported by Section 254(h), “the universal service contribution qualifies as a fee.” *Id.* at n. 52.

The court next dismissed Celpage’s Equal Protection claim in a single paragraph, concluding that “Celpage does not come close” to establishing that there is no reasonable relationship between the contributions telecommunications providers make to the universal service program and the benefits provided by the program. *Id.* at 428. It similarly disposed of Celpage’s “unconvincing takings claim,” explaining that Celpage had failed to establish any basis for the claim. *Id.* As this treatment indicates, the court of appeals was convinced that the four constitutional challenges to the schools and libraries program were totally lacking in merit.

The court found more merit to GTE’s argument that the Commission should not have provided support for internet access and internal connections, but ultimately rejected that argument too. GTE first argued that Section 254 permitted the Commission to authorize payments to support telecommunications services only. Thus, in GTE’s view, the program could support ordinary telephone service but not payments for internet access or the internal connections necessary to obtain internet access. The court found considerable support for GTE’s contentions, but also found that other evidence supported the Commission’s interpretation of Section 254(h). In particular, the court noted that Section 254(h)(2) directs the Commission to “enhance...access to advanced telecommunications and information services,” which plainly is something more than “plain old telephone service.” In addition, the court added, “some of the legislative history implies that Congress intended for subsection (h) to support internet access.” *Id.* at 442. The Fifth Circuit ultimately held that the Act is ambiguous with respect to this issue. Like the Supreme Court in *AT&T v. Iowa Utilities Board*, 119 S. Ct. 721 (1999), it concluded that “Congress realizes that many of these ambiguities will be resolved by the FCC during its implementation of the statute, and we, like the Court, generally defer to the agency’s interpretation.” Accordingly, the court “affirm[ed] those aspects of the Order providing internet services and internal connections to schools and libraries.” 183 F.3d at 443.

The court next rejected in summary fashion GTE's fallback argument that only telephone companies like itself—and not others, even if they provided superior service at lower prices—could receive support for providing internet access and internal connections. The court concluded that the Commission properly took “modest steps to ensure that Congress’s instructions on expanding universal service in the form of internet access and internal connections will not be frustrated by local monopolies.” *Id.* at 444. The court summarily rejected the argument that the Commission erred by conditioning its support for funding for intrastate services on the states’ establishing discounts equal to those authorized by the Commission for interstate services. *Id.* Similarly, the court found no merit at all to the contention that the Commission erred by authorizing discounts to schools and libraries for all commercially available telecommunications services; in GTE’s view, the Commission should have supported only a subset of telecommunications services. *Id.* at 445. And the court dismissed in a footnote the contention that support for internal connections may not be provided because they are “goods” rather than “services.” *Id.* at 441 n.88.

However, the court accepted Cincinnati Bell’s argument that the Commission erred by calculating assessments to the schools and libraries program on a carriers’ intrastate revenues as well as its interstate revenues. The court acknowledged that the Commission had given a reasonable reading to Section 254, but gave substantial weight to Section 152(b), which generally preserves authority over intrastate telecommunications issues not addressed by federal law to the state regulatory commissions, and concluded that carriers’ assessments should be based on their interstate revenues only. We filed a petition asking the en banc court to rehear that issue because the panel’s decision conflicts with the Supreme Court’s decision in the *Iowa Utilities Board* case, rendered earlier this year. The Court in that case addressed the “local competition” provisions of the Communications Act, which are Sections 251 through 261 of the Act and hence include Section 254. In our view, the court of appeals failed to heed Justice Scalia’s interpretation of Section 152(b), provided on behalf of the Supreme Court in that case. Justice Scalia explained that “the question is not whether the Federal Government has taken the regulation of local telecommunications competition away from the States. With regard to the matters addressed by the 1996 Act, it unquestionably has.” 119 S. Ct. at n. 6. He added that “[a]fter the 1996 Act, § 152(b) may have less practical effect. But that is because Congress, by extending the Communications Act into local competition, has removed a significant area from the States’ exclusive control.” *Id.* at n. 8. Other parties sought rehearing as well—but none on issues relating to the schools and libraries program. The court of appeals recently denied all of the petitions for rehearing. There is little doubt that the Supreme Court will be asked to review some aspects of this decision.

#### *Future Commission Action*

The Commission continues to work with the state members of the Joint Board and other parties to improve its rules regarding universal service so that the administration is as effective and efficient as possible, and so that support is set at the right levels and targeted to the appropriate schools and libraries. For example, the Commission will review by November 1999 its decision to name Universal Service Administrative Company (USAC) the permanent Administrator, to ensure that the support mechanisms are being administered “in an efficient, effective, and competitively neutral manner.” 47 C.F.R. § 54.701(a). The Commission also has committed to convening the Joint Board to review the definition of universal service on or before January 1, 2001. As Congress noted, universal service is an “evolving” level of services, and the Commission recognizes that there is always room for improvement to achieve all of the goals Congress set forth in section 254.

#### *H.R. 1746: Schools and Libraries Internet Access Act*

The Commission was charged by Congress with implementing Section 254, including the provisions that require universal service support for carriers that provide discounted services to schools and libraries. It has not been an easy task, and it certainly has not been without controversy. The Commission is pleased that the Fifth Circuit upheld most of the agency’s decisions regarding the schools and libraries support mechanism, and that at least the legal challenges to those decisions have apparently been laid to rest. It took a long time to get this far—three and a half years after Congress enacted Section 254 and more than two years since the Commission issued its initial Report and Order on universal service. But today, the schools and libraries support mechanism is up and running, and providing benefits to schools and libraries in every state.

The proposed legislation, H.R. 1746, appears to be consistent with many of the goals of the schools and libraries and rural health care support mechanisms set forth in section 254. It seems clear that the substantive goal—making sure that schools, libraries, and health care providers have affordable access to telephone and other communications services—is not being questioned, and that the real debate is how, administratively, to achieve that goal. However, the proposed bill is not without ambiguity, and the Commerce Department would need to resolve that ambiguity in implementing the bill and then in defending its interpretation in the face of the judicial challenges that are likely to follow. For example, although it seems reasonably clear that the provision is designed to provide support for internet access and internal connections, like the existing program, the bill does not use those words, but instead speaks of “telecommunications and related services.” Accordingly, opponents of connecting schools to the internet may raise some of the same objections that they raised to the Commission’s implementation of Section 254(h). Similarly, the bill speaks of equipment “essential to permit...access to advanced technologies.” It is not clear whether the use of the word “essential” is meant to require the use of a stricter standard than is currently employed in reviewing requests by schools and libraries for internal connections and, if so, what that standard is. Unless matters such as these are clarified, another round of litigation and uncertainty may follow.

In light of the Fifth Circuit’s decision rejecting the challenges to the Commission’s rules regarding the schools and libraries program, there is no legal need to modify the current method of administration in order to provide support to schools and libraries seeking assistance in obtaining internet connections. Thus, the question before Congress is a policy decision. Congress must determine whether the benefits of a different method of administration will outweigh the difficulties that starting afresh might create. Whatever decision Congress makes with respect to the administration of universal service, the Commission, of course, will continue to work diligently to satisfy its responsibilities.

I would be happy to answer any questions that you and any other members of the Subcommittee may have.

Mr. TAUZIN. Thank you very much, Mr. Wright. And next will be Kelly Levy, Acting Associate Administrator of the Office of Policy Analysis, NTIA, of the Department of Commerce. Ms. Levy.

#### STATEMENT OF KELLY KLEGAR LEVY

Ms. LEVY. Thank you, Mr. Chairman. Good morning. On behalf of the administration, I want to thank you and the other members of the subcommittee for having me up here today. It is an honor. Thank you for letting us testify on H.R. 1746, the Schools and Libraries Internet Access Act.

Mr. Chairman and members of the subcommittee, the administration shares your goal of providing advanced telecommunications services to schools and libraries. Both President Clinton and Vice President Gore have made connecting schools and libraries to the Nation’s information infrastructure one of their highest priorities. As the President stated, until every child has a computer in the classroom and the skills to use it, until every student can tap the enormous resources of the Internet, until every high-tech company can find the skilled workers to fill high-wage jobs, America will miss the full promise of the Information Age.

The administration strongly supported section 254(h) of the Telecommunications Act of 1996, which established the E-Rate program as part of the overall universal service fund. And the administration has supported full funding of that program.

Today, the E-Rate program is helping to connect schools and libraries at a very rapid pace. For instance in the first year of the program, over 640,000 classrooms were connected to the Internet. Importantly, the E-Rate program gives priority funding to poor and rural schools and libraries. Mr. Chairman, NTIA shares your con-

cern that the schools and libraries program be administered expertly, efficiently and impartially. However, we see no need for new legislation to change the E-Rate program in order to bring the full promise of the Information Age to our children.

Congressional oversight, including input from the House Commerce Committee, and a two-tiered auditing process have helped to ensure that the Universal Service Administrative Company, USAC, is running the E-Rate program efficiently and that schools and libraries are using E-Rate money to fund only eligible services.

H.R. 1746, the Schools and Libraries Internet Access Act, would establish NTIA as the administrator of the universal service program for schools and libraries as well as health care providers. NTIA believes that it is premature to consider such a drastic measure. First, we believe that the third-party nongovernmental entities have a commendable performance record in this regard. While the USAC may have experienced some startup difficulties, we believe that it has taken the appropriate corrective actions.

Second, in the competitive environment, many believe that the fund administrator must not advocate telecommunications policy positions, a role that would be incongruous with NTIA's existing statutory mandate.

Third, as fund administrator, NTIA would incur large startup costs, costs that have already been incurred by the USAC. In its current operating mode, NTIA does not possess the resources or the infrastructure to run the proposed E-Rate program. In addition, last year the administration, through a letter from the Office Management and Budget to Chairman Tauzin as well as to Senator Burns, also raised significant budget issues on similar legislation that was before this subcommittee last year.

Finally, our greatest concern is that any fundamental change in the administration of the E-Rate program will delay and even forfeit opportunities for our children.

In conclusion, as Secretary of Commerce William Daley has stated: Tomorrow's economy will demand technological literacy. The E-Rate program is an important step to ensure that our economy grows strongly and that in the future no one is left behind.

Thank you again for the opportunity to testify and I am pleased to answer any questions you may have.

[The prepared statement of Kelly Klegar Levy follows:]

PREPARED STATEMENT OF KELLY KLEGAR LEVY, ACTING ASSOCIATE ADMINISTRATOR,  
OFFICE OF POLICY ANALYSIS AND DEVELOPMENT, NATIONAL TELECOMMUNICATIONS  
AND INFORMATION ADMINISTRATION, U.S. DEPARTMENT OF COMMERCE

Mr. Chairman and Members of the Subcommittee: Thank you for this opportunity to testify this morning, setting forth the views of the National Telecommunications and Information Administration (NTIA) with respect to H.R. 1746, the Schools and Libraries Internet Access Act. NTIA serves as a principal adviser to the President, Vice President, and Secretary of Commerce on domestic and international telecommunications and information policy issues and has been an active participant in the schools and libraries support process.

The Administration shares your goal of providing advanced telecommunications services to schools and libraries. Both President Clinton and Vice President Gore have made connecting schools and libraries to the nation's information infrastructure one of their highest priorities. The importance of enabling schools, including classrooms, and libraries to access the Internet, in conjunction with an integrated, well-developed curriculum, cannot be overstated. As the President stated: "Until every child has a computer in the classroom and the skills to use it...until every

student can tap the enormous resources of the Internet...until every high-tech company can find skilled workers to fill its high-wage jobs...America will miss the full promise of the Information Age." Once viewed with curiosity, the information revolution has brought fundamental changes to the fabric of society and to the foundations of the emerging global economy.

In June 1999, the Department of Commerce released *The Emerging Digital Economy II*, a report that demonstrated the increasingly pivotal role that information technologies play in our economy and the dramatic growth of electronic commerce. In July 1999, the Department of Commerce released *Falling Through the Net: Defining the Digital Divide*, a report examining which American households have access to key information tools—telephones, computers, and the Internet—and which do not. Overall, we found that more Americans than ever before own computers and are online. At the end of 1998, over 40 percent of American households owned computers, and almost one-quarter of all households had Internet access.

Yet, *Falling Through the Net* also documented that there remains a significant digital divide separating American information "haves" and "have nots." Indeed, in many instances, the digital divide has widened in the last year. Certain minorities, low-income persons, the less educated, and children of single-parent households, particularly when they reside in rural areas or central cities, are among the groups that lack access to information resources. Because access to computers and the Internet is increasingly critical to successful participation in our digital economy, we need to ensure that everyone has access to these technologies.

One of the interesting findings of *Falling Through the Net* is that community access centers—such as schools, libraries, and other public access points—are particularly well used by those groups that lack access at home or at work. For example, Hispanics and American Indians/Eskimos/Aleuts are especially likely to use schools for access if they live in rural areas. Households with incomes less than \$25,000, those with less than a high-school education, those in female-headed households, and American Indian/Eskimos, Aleuts, Blacks, and Hispanics who have low Internet access rates at home are relying with a great deal of frequency on public libraries for access to the Internet.

Thus, the *Falling Through the Net* data underscore the importance of efforts by Congress, as well as the Administration, to ensure that all schools and libraries have affordable access to the Internet on sustained basis. The Administration strongly supported Section 254(h) of the Telecommunications Act of 1996, which established the E-rate program as part of the overall Universal Service Fund. And the Administration has supported full funding of that program. Under the E-rate program, telecommunications carriers are providing eligible schools and libraries with a discounted rate for telecommunications services, internal connections among classrooms, and Internet access. As a result, the E-rate program is helping to connect schools and libraries at a very rapid pace. In the first year of the program, 640,000 classrooms were connected to the Internet. This year, \$2.25 billion is available to connect an expected 528,000 additional classrooms. Eighty percent of public schools and fifty percent of public libraries participate in the E-rate program. Importantly, the E-rate program gives priority for funding to poor and rural schools and libraries.

Moreover, the E-rate monies are proving to be a catalyst for other efforts to connect schools and libraries to online resources. Many states and communities are combining the Federal E-rate funds with state and/or private sector money to address access problems. In Louisiana, for example, \$500,000 in E-rate funding received by the State Library of Louisiana combined with \$2 million in state funding and \$7 million from the Gates Library Foundation will enable the state library to provide Internet access and computers for every library in the state. While just three years ago many parts of Louisiana were entirely cut off from the Internet, now every library in the state has computers and Internet access, which are available for free to all 4.3 million residents.

The American public joins us in strongly supporting the E-rate program. As information technology becomes increasingly important in our global economy, Americans have come to overwhelmingly support the need for computers in our nation's classrooms and libraries. A non-partisan poll commissioned by EdLiNC found that 87 percent of respondents support the mission of the E-rate program. The public's support of the E-rate program is echoed by parent and teacher groups, library organizations, high-tech companies, many telecommunications providers, and civil rights groups.

On July 30, 1999, the Fifth Circuit Court upheld the structure of the E-rate program, including coverage for Internet access and connections to the classroom as well as telecommunications services, and upheld the Federal Communications Commission's authority to target discount levels to the schools and libraries with great-

est needs. Now with the court case behind us, we hope that this program can achieve its full potential.

Mr. Chairman, NTIA shares your concern that the schools and libraries program be administered expertly, efficiently, and impartially. However, we see no need for new legislation to change the E-rate program in order to bring the full promise of the Information Age to our children. Congressional oversight, including input from the House Commerce Committee, and a two-tiered auditing process have helped to ensure that the Universal Service Administrative Company (USAC) is running the E-rate program efficiently, and that schools and libraries are using E-rate money to fund only eligible services. Moreover, the E-rate program is part of Universal Service—a program that, for the vast majority of Americans, has worked well for over 60 years.

H.R. 1746, the Schools and Libraries Internet Access Act, would establish NTIA as the administrator of the universal service program for schools and libraries as well as rural health care providers. NTIA believes that it is premature to consider such a drastic measure. First, we believe that third-party, non-governmental entities have a commendable performance record in this regard. While the USAC may have experienced some start-up difficulties, we believe that they have taken the appropriate corrective actions. More time is needed to allow the system to work. Second, in the new competitive environment, many believe that the fund administrator must not advocate telecommunications policy positions, a role that would be totally antithetical to, and incongruous with, NTIA's existing statutory mandate. Third, as fund administrator, NTIA would incur large start-up costs—costs that have already been incurred by the USAC. In its current operating mode, NTIA does not possess the resources or infrastructure to run the proposed E-rate grant program. While we feel confident that we could administer the fund on an impartial basis and do so in an accountable manner, these factors would not offset the above disadvantages. In addition, the Administration, through a letter from the Office of Management and Budget to Chairman Tauzin, as well as to Senator Burns, also raised significant budget issues on similar legislation before this subcommittee last year.

Aside from these issues, our greatest concern is that any fundamental change in the administration of the E-rate program will delay and forfeit opportunities for our children. Delay denies students and teachers access to information and telecommunications technologies and their benefits. Research shows that technology can enhance learning opportunity and achievement, increase student motivation to learn, help students acquire essential workplace skills, improve professional development for teachers, and enable students to access high-quality education regardless of time or place. As Vice President Gore has noted, “[f]or the very first time in our history, it is now possible for a child in the most isolated inner-city neighborhood or rural community to have access to the same world of knowledge at the same instant as the child in the most affluent suburb.”

Another recent Commerce Department report, *The Digital Work Force: Building Infotech Skills at the Speed of Innovation*, stresses the importance of expeditiously meeting the burgeoning demand for a highly-skilled labor force. In testimony before the Congressional Joint Economic Committee, such notables as Federal Reserve Board Chairman Alan Greenspan, Bill Gates, and many other leaders from the technology industry have testified not only that technology has played a leading role in building and strengthening our economy but also that the foundation for this growth is a quality education for every student. If students—and others—cannot obtain the high-tech skills and ready access to information that is critical for success in the emerging digital economy, then our nation's ability to compete and prosper will be put at risk. Particularly hard hit would be students at the disadvantaged schools and libraries—those in low-income, rural, or inner-city areas who likely would have to do without Internet access unless universal service support is made available.

As Secretary of Commerce William Daley has noted, “[t]omorrow's economy will demand technological literacy—the E-rate is an important step to ensure that our economy grows strongly and that in the future no one is left behind.” During its evolution, the E-rate program has already demonstrated its value, and the Administration continues its strong support for the existing program and its goals. Thank you again for the opportunity to testify.

Mr. TAUZIN. Thank you very much. Next will be Dr. Lois Gerber, Chairman of the Board of the National Independent Private Schools Association.



**STATEMENT OF LOIS M. GERBER**

Ms. GERBER. Thank you, Mr. Chairman. You know it is a real challenge for an educator to have 5 minutes but I will do the best I can.

The organization that I represent is fast becoming a minority in this group, and you, yourself, have said that you wish not to establish or leave out or make another minority. But, unfortunately, Schools and Libraries Internet Access Act is using as definition what the Elementary and Secondary Act of 1965 described as "school."

Now, many of you perhaps were not as old as I am and you don't remember that act but that act was developed on child benefit and we have talked this morning and we have heard about child benefit. I have heard all children, every school.

Unfortunately, there are a group of children, 50,000 which I represent and probably 100,000 more out there, that are being eliminated because you are using the Child Benefit Act description of schools that the regulators then took that act and described what a school was. A school according to the Department of Education in America is a public school, a nonprofit school or a parochial school.

In 1965, there were very few taxpaying schools in this country. Most of them were vocational. However, since then we all know life in the world has changed and so has the world of education. We now have a viable organization that I represent that are all taxpaying academic schools.

Most of us are family owned businesses but we have multischools and corporations also. Most of us are nonselective in the type of children that we put into our schools. 30 percent of us have learning disabled children, physically challenged children. Our school particularly, the one that my husband and I own, have mentally challenged children. And we take children—we give millions of dollars a year in scholarships to disadvantaged children because the only thing that our schools offer is education. We do not have any reason for a parent to come to our school except for the product of education.

It is our job to keep that level of product at a point that they can afford. Everything we do in our schools are tuition driven. And yet on the other end we have chosen to take this financial risk to prove that education can work, that we can serve the children that wish to come, and yet we pay millions of dollars in property taxes, sales taxes and corporate taxes and get nothing in return.

Now, this is an interesting position for me to be in because usually when I come up on the Hill and Members of Congress ask me what we want I keep saying we really don't want anything, please don't bother us. But in this case we do. We want the definition of what a school in America is to change. We want you to realize that if you keep that definition in the Schools and Libraries Internet Access Act, you are literally disenfranchising our children. What we are asking for is for them to have it. We are not asking for a business advantage but we are asking help to provide for our children those services that all other children in all schools are being provided.

You see by keeping that definition, it infers all nonprofit schools are good and anything else is not good. And yet the Immigration and Naturalization Service has said that they accept accredited schools as schools able to not have to go through a curriculum review in order to give student visas. Our accreditation has been accepted and approved and scrutinized by the National Council for Private School Accreditation. We are working in a partnership with all the regional organizations to form the International Academy of School Accreditors.

My point is this, that accreditation and viable accreditation is a much better way to say whether a school is viable than to lump them into nonprofit or for-profit schools. Secretary Riley said this, he said it in 1996 when he said the administration's goal was for all children to have access. Well, all we would like to say is that there are no nonprofit and for-profit children in this country to educate. We all educate children and our children do not want to become the next educational minority of this country. Thank you and I would love to answer any questions.

[The prepared statement of Lois M. Gerber follows:]

PREPARED STATEMENT OF LOIS M. GERBER, CHAIRMAN OF THE BOARD, NATIONAL  
INDEPENDENT PRIVATE SCHOOLS ASSOCIATION

Thank you Mr. Chairman and Members of the Committee. As Chairman of the Board of the National Independent Private Schools Association. Commonly known as NIPSA and Co-owner and Co Director of Bradenton Academy in Bradenton Florida. It is my pleasure to be here today to discuss with you an inequity in the proposed legislation. That is the inclusion of schools, but only those as defined in the Elementary and Secondary Appropriation bill.

The time has come in America that we begin to look at our definition of schools public and private. Although public schools have become the primary source of education in the United States, it was not always that way. In fact, the first schools in the United States were privately owned. Our founding Fathers relied on free enterprise to educate the youth of their new nation. Almost 200 years later, The National Independent Private Schools Association (NIPSA) was founded to represent the virtues of educational choice and high academic standards. All NIPSA members are private, tax-paying, academic, non-religiously affiliated independent institutions located in both urban and suburban areas throughout the country. These elementary and secondary schools are run by proprietors who believe strongly that education can be made better and they are willing to assume all the financial and operating risks associated with running a private school. These dedicated educators have met this challenge while maintaining the highest education standards. In the process of doing this, NIPSA members have also kept the doors open to all children. Many of our members have made significant contributions to public education at earlier stages in their careers, ie. Some have been superintendent of schools and administrators.

Mr. Chairman and Members of this distinguished Committee, I respectfully ask that you review today: *Section 106.6A DEFINITION—For purposes of this section: (A) ELEMENTARY AND SECONDARY SCHOOLS—The terms 'elementary and 'secondary school' have the same meanings given those terms in paragraphs (14) and (25), respectively, of section 14101 of the Elementary and Secondary Education Act of 1965.*

The Elementary and Secondary Education Act of 1965 was funded on the basis of "child benefit". It was when the regulators wrote the rules that we began this stipulation of funding only public and non-profit schools. If you continue on the premise that you are funding education on "Child Benefit" but by definition of the regulators, you have excluded 50,000 children in NIPSA and probably another 100,000 that are in unaffiliated schools. This is an unintentional oversight but an oversight just as well.

Let me explain the logic of why NIPSA children should be included in this Act cited as "Schools and Libraries Internet Access Act".

There are four significant traits of all NIPSA Member Schools:

- Accreditation—All member schools undergo a stringent NIPSA accreditation process which has been reviewed and accepted by the National Council for Private School Accreditation;
- Accountability—Teachers and staff gladly understand that if their school does not provide a quality education for students, the school will be forced to close its doors. Parents simply will not continue sending their children to NIPSA schools;
- Financial management expertise—In order to remain viable, NIPSA schools have learned proper budgeting, inventory control, regulation of administrative costs, and prudent purchasing strategies;
- Emphasis on children—All NIPSA schools are singularly focused on building students not administrative organizations-administrative staff is kept to a minimum, classroom size is kept small, decisions are made on-site.

NOIPSA schools are, in essence, true educational schools of choice, with a sole funding source-parents. We receive no federal funds, endowments, foundation funds or donations. Our schools are held to the highest accountability standards because, in a free market, schools that deliver a quality educational product at an affordable price become successful schools while schools that deliver poor educational results go out of business.

NIPSA schools provide before and after-school care, summer programs, scholarships for disadvantaged children, and most importantly many are dedicated to educating that segment of the school population that has been termed as "high-risk". Thirty percent of our schools enroll children with learning disabilities, one percent have physically challenged youngsters, and ninety-five percent have programs for gifted learners.

Perhaps one of the most important factors to consider is that NIPSA schools are tax paying schools. We contribute to the tax base of this country that is contributing these grants to schools that are public or non-profit. Our schools pay property taxes, sales taxes and millions in corporate income taxes. There should be some benefit for our students. We are not asking for help in managing our business or in any area that would give us a business advantage. It is difficult enough, to provide quality education, professional staff and all of the necessary materials plus housing for students when the income for all of this is tuition driven. We are dedicated to continuing this however we wish to provide our students with the library and internet access at a reasonable educational fee, not a commercial rate.

Finally, let me quote Secretary of Education Richard Riley. Speaking at a teleconference in San Diego in 1996, he noted that schools and libraries were already making big investments in technology. He reminded Reed Hundt, the chairman of the FCC, that under the administration proposal, ALL k-12 schools public and private and parochial schools, as well as public libraries, would receive a basic package of services for free. He closed by reminding the board further that, "The proposal advances the long-standing American tradition of providing free education and free access to libraries to EVERY AMERICAN CHILD".

I respectfully submit to this distinguished Committee that America does not have nonprofit children and for profit children. We have children to educate. Thank you for your consideration.

Mr. TAUZIN. Thank you very much. Next Ms. Cheryl Parrino, the CEO of the USAC corporation. Ms. Parrino.

#### STATEMENT OF CHERYL PARRINO

Ms. PARRINO. Good morning. It is a pleasure to be here with you today representing the Universal Service Administrative Company and to share with you a bit of information about the administration and our work of administering the four funds that were established by the FCC in response to the Telecom Act of 1996.

As you recall, Congress authorized four universal service programs, the High Cost Program, Low-Income, Rural Health Care, and Schools and Libraries. USAC is charged with administering all four of those programs.

The High Cost Program that was mentioned earlier today by Congressman Markey provides support primarily to high cost areas, rural areas of this country, and we fund those entities to the tune of about \$1.7 billion on an annual basis.

Attachment A to my testimony provides you information for each of the parts of that program on a State-by-State basis, how much money is distributed across the country under the High Cost Program.

We also administer the Low-Income Program which provides opportunities or subsidies for low-income customers to be able to hook up to the telephone and help buy down their monthly rates. About 5 million customers across the United States have taken advantage of that program in 1998 and we have funded those customers to the tune of about \$500 million.

Attachment B, again State by State for each component of the program, it gives you information on how much money has been distributed in 1998 for the Low-Income Program.

The third program is the Rural Health Care Program, which provides subsidies to buy down the difference between the rural and urban rate so that rural health care providers can use technology to provide health services to rural parts of this country. To the extent that the High Cost Program has been very successful in balancing or equalizing the rates between urban and rural places in this country, that has minimized the impact of that program. But in the first year we had an indication of interest from about 2,800 rural health care providers. About 600 of those have filed complete applications and to date we have funded about \$1 million to 170 eligible rural health care providers in 34 States. Attachment C provides you with the same sort of information as the previous attachments for that program.

Last but not least, the Schools and Library Program, which is the primary subject of this hearing today, is also administered by USAC. In the first year we received more than 30,000 applications. We supported 25,785 applicants representing public and private schools and public libraries up to the FCC cap of \$1.9 billion for the first 18 months of the program.

Again, attachment D provides you information for the Schools and Libraries Program.

In year two we have received 32,000 applications and we will fund up to the FCC cap of \$2.25 billion.

As you well know, USAC's mandate is a very narrow one. We have been charged with administering the four universal service programs I have described. USAC charter from the FCC strictly limits our role. USAC cannot and does not establish policy or advocate any position before the FCC or Congress. Over the past 2 years we have hired independent auditors Price Waterhouse Coopers and Deloitte Touche to assist us in designing efficient operating procedures for the new programs. Each of these firms have attested that our procedures are efficient and suitable, designed to prevent or detect any material departures from program objectives.

We have also been given a clean bill of health by Arthur Andersen in our 1998 financial and operational audits. At direction of Senator McCain, the General Accounting Office reviewed the procedures of the Schools and Libraries Division and observed in their July 16 testimony that the Schools and Libraries Division has made substantial progress in establishing an operational framework for the program that is consistent with the relevant FCC orders.

I thank you. Again I would like to highlight that I am not able to, given my narrow charge, I am not able to comment on your bill, but I would be happy to answer any questions you may have about the program.

[The prepared statement of Cheryl Parrino follows:]

PREPARED STATEMENT OF CHERYL PARRINO, CHIEF EXECUTIVE OFFICER, UNIVERSAL SERVICE ADMINISTRATIVE COMPANY

Good morning, Mr. Chairman and Members of the Committee. It is my privilege to be here today to speak to you about the Universal Service Administrative Company (referred to as USAC) and our administration of the universal service programs as established by the FCC as a result of the Telecommunications Act of 1996.

As you will recall, Congress authorized four universal service programs: the High Cost Program, the Low Income Program, the Schools and Libraries Program, and the Rural Health Care Program. I would like to very briefly describe the programs as they exist today and provide you with information concerning the benefits that are being provided.

**The High Cost Program** provides support to Eligible Telecommunications Carriers (companies) who deliver basic "core" telephone service to customers in areas of the country that are more costly to serve. There are three parts of the High Cost program which help companies deliver telephone service to all Americans. The High Cost Loop portion covers the cost of the last mile to the customer if it is 115% greater than the national average, the Local Switching Support portion of the fund covers switching costs for small companies that serve less than 50,000 customers, and the Long Term Support portion helps offset access charge rates charged by small and predominately rural companies. In 1998, USAC provided approximately \$1.7 billion in High Cost support. Attachment A provides detail for each state, each portion of the program and the total high cost funding for 1998.

**The Low Income Program** helps make telephone service more affordable for low-income consumers through two national programs, Lifeline and Link-Up. Approximately 5 million customers have taken advantage of this program. The Lifeline program helps to offset the monthly bill and the Link-Up program helps to offset the one-time hookup or connection charge. The program will also pay for the cost of toll blocking which helps the customer control the phone bill. In 1998, USAC provided approximately \$465 million in Low Income Universal Service support to Eligible Telecommunications Carriers to offset charges on low-income consumers' bills. Attachment B provides detail for each state, each portion of the program and the total low income funding for 1998.

**The Rural Health Care Program** provides support to rural health care providers to ensure that they pay no more than their urban counterparts for telecommunications services. Support applies to monthly telecommunications service charges, installation charges, and long distance charges for access to the Internet. During the first year of the program, 2835 rural health care providers indicated an interest in the program and 616 submitted applications for support. To date almost \$1 million has been committed to 170 eligible rural health care providers in 34 states. The Rural Health Care Division continues to process Year 1 applications. Attachment C provides a summary of the funds committed thus far for Year 1.

**Finally**, the Schools and Libraries Program (commonly referred to as the E-Rate) helps provide affordable access to telecommunications services for all eligible schools and libraries, particularly those in rural and economically disadvantaged areas. The program provides discounts of 20% to 90% on telecommunications services, Internet access and internal connections. The level of discounts that schools and libraries are eligible to receive depends on economic need and location, rural or urban. More than 30,000 applications were received during the first year of the program. Support was provided to 25,785 applicants representing public and private schools and public libraries up to the FCC cap of \$1.9 billion for the first 18 months of the program. For your reference, Attachment D provides a summary of the funding commitments that were made for Year 1. In Year 2 we have received 32,000 applications. USAC will fund eligible requests up to the \$2.25 billion cap established by the FCC.

USAC's mandate is a narrow one. We have been charged with administering the four universal service programs I have briefly described. The USAC charter from the FCC strictly limits our role. USAC cannot and does not establish policy or advocate any position before the FCC or Congress. Since its creation in September of 1997, USAC has worked hard to increase its efficiency and effectiveness. On January 1, 1999, as ordered by the FCC, the Rural Health Care Corporation and the Schools and Libraries Corporation merged into USAC. The merger has resulted in

an initial savings of 10%. We continue to look for efficiencies and additional opportunities for streamlining.

In summary, USAC has worked diligently to ensure that the programs are administered in accordance with the rules promulgated by the Federal Communications Commission. As the administrator of these programs, USAC has no authority to advocate policy and therefore I cannot take a position on HR 1746. I would however be pleased to respond to any questions you may have about the programs or USAC.

#### ATTACHMENT A

#### Universal Service Administrative Company High Cost Program

Total Projected Support Payments for 1998 by State

State or Jurisdiction	Universal Service Fund	Long Term Support	Local Switching Support	Total Support
ALABAMA .....	\$21,947,616	\$6,812,558	\$10,153,266	\$38,913,440
ALASKA .....	\$31,963,777	\$16,287,535	\$14,909,157	\$63,160,470
ARIZONA .....	\$19,492,163	\$2,996,004	\$7,785,833	\$30,274,001
ARKANSAS .....	\$46,089,633	\$14,974,038	\$9,584,889	\$70,648,560
CALIFORNIA .....	\$28,886,748	\$15,252,293	\$8,255,564	\$52,394,605
COLORADO .....	\$29,084,089	\$12,480,408	\$4,354,619	\$45,919,116
CONNECTICUT .....	\$0	\$173,885	\$1,229,387	\$1,403,271
DELAWARE .....	\$0	\$0	\$0	\$0
DISTRICT OF COLUMBIA .....	\$0	\$0	\$0	\$0
FLORIDA .....	\$11,300,827	\$6,216,006	\$4,622,852	\$22,139,686
GEORGIA .....	\$41,660,333	\$17,469,442	\$12,673,651	\$71,803,426
GUAM .....	\$0	\$1,036,397	\$0	\$1,036,397
HAWAII .....	\$0	\$253,710	\$645,216	\$898,926
IDAHO .....	\$19,505,787	\$2,651,783	\$6,406,782	\$28,564,351
ILLINOIS .....	\$5,717,032	\$5,260,687	\$11,745,592	\$22,723,310
INDIANA .....	\$2,922,762	\$5,051,789	\$8,062,461	\$16,037,012
IOWA .....	\$5,682,281	\$7,444,862	\$16,926,049	\$29,053,192
KANSAS .....	\$36,263,126	\$9,228,572	\$12,687,975	\$58,179,674
KENTUCKY .....	\$14,146,447	\$5,274,410	\$5,764,233	\$25,185,091
LOUISIANA .....	\$41,626,484	\$17,112,419	\$8,025,003	\$66,763,905
MAINE .....	\$5,142,391	\$5,566,003	\$6,145,029	\$16,853,424
MARYLAND .....	\$0	\$93,174	\$497,916	\$591,089
MASSACHUSETTS .....	\$6,686	\$89,836	\$270,257	\$366,779
MICHIGAN .....	\$13,982,051	\$8,628,866	\$10,042,616	\$32,653,533
MINNESOTA .....	\$8,924,455	\$11,401,747	\$18,068,447	\$38,394,648
MISSISSIPPI .....	\$18,338,576	\$4,903,515	\$4,226,669	\$27,468,760
MISSOURI .....	\$29,578,017	\$10,545,430	\$9,463,755	\$49,587,202
MONTANA .....	\$23,467,678	\$9,989,579	\$9,693,921	\$43,151,178
NEBRASKA .....	\$6,281,317	\$3,723,244	\$10,408,820	\$20,413,381
NEVADA .....	\$3,252,723	\$1,029,177	\$4,789,246	\$9,071,146
NEW HAMPSHIRE .....	\$2,473,619	\$1,583,426	\$4,873,081	\$8,930,126
NEW JERSEY .....	\$2,012,385	\$0	\$1,097,875	\$3,110,260
NEW MEXICO .....	\$19,260,613	\$5,929,144	\$9,278,954	\$34,468,711
NEW YORK .....	\$10,664,865	\$7,008,888	\$18,238,267	\$35,912,019
NORTH CAROLINA .....	\$21,836,970	\$13,015,756	\$6,240,669	\$41,093,395
NORTH DAKOTA .....	\$5,074,893	\$5,440,606	\$11,023,045	\$21,538,543
NORTHERN MARIANA ISLANDS .....	\$3,601,484	\$0	\$1,332,414	\$4,933,899
OHIO .....	\$4,476,642	\$5,189,569	\$5,023,827	\$14,690,038
OKLAHOMA .....	\$27,353,330	\$15,826,197	\$15,833,411	\$69,012,937
OREGON .....	\$18,563,458	\$10,471,338	\$7,584,140	\$36,618,937
PENNSYLVANIA .....	\$1,383,836	\$14,037,268	\$8,771,332	\$24,192,436
PUERTO RICO .....	\$48,786,061	\$93,890,023	\$0	\$142,676,084
RHODE ISLAND .....	\$0	\$0	\$0	\$0
SOUTH CAROLINA .....	\$23,680,509	\$9,971,023	\$12,919,526	\$46,571,058
SOUTH DAKOTA .....	\$3,160,201	\$4,331,610	\$10,412,199	\$17,904,010
TENNESSEE .....	\$8,152,076	\$9,452,075	\$10,515,599	\$28,119,750
TEXAS .....	\$75,837,949	\$29,658,890	\$19,282,803	\$124,799,642
UTAH .....	\$2,981,619	\$1,268,015	\$4,761,353	\$9,010,987
VERMONT .....	\$4,144,186	\$3,291,398	\$4,766,929	\$12,202,512
VIRGIN ISLANDS .....	\$11,315,559	\$4,935,577	\$0	\$16,251,136
VIRGINIA .....	\$4,780,376	\$3,348,990	\$5,225,657	\$13,355,023
WASHINGTON .....	\$23,442,891	\$12,470,927	\$6,955,915	\$42,869,733

## Universal Service Administrative Company High Cost Program—Continued

Total Projected Support Payments for 1998 by State

State or Jurisdiction	Universal Service Fund	Long Term Support	Local Switching Support	Total Support
WEST VIRGINIA .....	\$17,173,230	\$1,069,241	\$3,064,611	\$21,307,082
WISCONSIN .....	\$13,108,671	\$13,716,424	\$24,465,366	\$51,290,461
WYOMING .....	\$22,501,742	\$4,082,462	\$4,528,568	\$21,112,772
INDUSTRY .....	\$831,030,165	\$471,936,214	\$412,634,743	\$1,715,601,122

## ATTACHMENT B

## Universal Service Administrative Company Schedule of Low Income Program Dollars

January-December 1998

State or Jurisdiction	Lifeline	Linkup	TLS	PICC	Total
ALABAMA .....	\$1,416,925	\$37,716	\$2,119	\$16,305	1,473,065
ALASKA .....	188,578	17,367	14,584	60	220,589
AMERICAN SOMOA .....	8,167	3,660	0	0	11,827
ARIZONA .....	1,100,289	12,446	13,621	1,035	1,127,391
ARKANSAS .....	579,799	141,989	2,837	4,832	729,457
CALIFORNIA .....	243,424,958	28,644,537	1,938,526	1,259,338	275,267,359
COLORADO .....	1,830,137	44,217	18,578	8,345	1,901,277
CONNECTICUT .....	3,611,946	201,089	27,447	21,318	3,861,800
DELAWARE .....	23,198	2,376	0	0	25,574
DISTRICT OF COLUMBIA .....	0	0	0	0	0
FLORIDA .....	10,035,286	196,450	9,789	70,479	10,312,004
GEORGIA .....	6,129,291	204,596	8,052	49,896	6,391,835
GUAM .....	18,061	3,521	0	0	21,582
HAWAII .....	551,000	34,784	0	150	585,934
IDAHO .....	567,496	11,509	3,877	1,000	583,882
ILLINOIS .....	1,832,182	317,772	995	17,291	2,168,240
INDIANA .....	782,948	103,698	1,527	9,888	898,061
IOWA .....	146,995	28,639	10,959	1,815	188,408
KANSAS .....	336,607	26,737	993	1,822	366,159
KENTUCKY .....	304,340	143,819	4,200	5,307	457,666
LOUISIANA .....	366,692	73,810	1,433	10,857	452,792
MAINE .....	5,284,914	476,938	19,660	19,402	5,800,914
MARYLAND .....	319,809	0	0	0	319,809
MASSACHUSETTS .....	13,572,243	108,720	0	55,882	13,736,845
MICHIGAN .....	9,676,719	384,007	8,773	73,502	10,143,001
MINNESOTA .....	3,505,814	15,793	3,233	932	3,525,772
MISSISSIPPI .....	876,569	38,181	1,234	9,295	925,279
MISSOURI .....	545,922	83,766	2,683	2,062	634,433
MONTANA .....	665,191	20,099	10,524	1,945	697,759
NEBRASKA .....	585,475	8,380	12,640	3,411	609,906
NEVADA .....	214,009	1,875	410	13	216,307
NEW HAMPSHIRE .....	161,458	26,155	0	873	188,486
NEW JERSEY .....	317,378	22,502	149	0	340,029
NEW MEXICO .....	2,494,090	116,219	70,603	31,716	2,712,628
NEW YORK .....	53,778,248	5,479,060	19	969,876	60,227,203
NORTH CAROLINA .....	2,412,287	38,516	1,971	13,365	2,466,139
NORTH DAKOTA .....	853,729	23,136	10,603	4,525	891,993
NORTHERN MARIANA ISLANDS .....	10,659	5,887	0	0	16,546
OHIO .....	5,231,163	319,261	20,325	99,255	5,670,004
OKLAHOMA .....	104,641	47,836	883	928	154,288
OREGON .....	2,328,845	44,007	19,739	10,280	2,402,871
PENNSYLVANIA .....	1,689,112	898,486	90	800	2,588,488
PUERTO RICO .....	587,156	68,116	0	0	655,272
RHODE ISLAND .....	3,753,152	29,878	0	23,846	3,806,876
SOUTH CAROLINA .....	1,794,933	42,388	6,278	21,106	1,864,705
SOUTH DAKOTA .....	647,158	29,448	15,138	3,267	695,011
TENNESSEE .....	1,862,505	78,042	1,364	10,248	1,952,159
TEXAS .....	17,075,909	2,243,803	173,804	161,996	19,655,512
UTAH .....	1,665,225	36,078	24,856	9,191	1,735,350

Universal Service Administrative Company Schedule of Low Income Program Dollars—Continued  
January-December 1998

State or Jurisdiction	Lifeline	Linkup	TLS	PICC	Total
VERMONT .....	2,207,827	24,157	487	2,958	2,235,429
VIRGIN ISLANDS .....	49,229	2,005	0	0	51,234
VIRGINIA .....	1,772,255	27,350	474	627	1,800,706
WASHINGTON .....	4,029,780	409,930	89,905	33,236	4,562,851
WEST VIRGINIA .....	367,781	1,280	0	23	369,084
WISCONSIN .....	2,715,202	376,880	3,037	48,748	3,143,867
WYOMING .....	92,637	424	456	127	93,644
<b>TOTALS .....</b>	<b>\$416,503,919</b>	<b>\$41,779,335</b>	<b>\$2,558,875</b>	<b>\$3,093,173</b>	<b>\$463,935,302</b>

SOURCE: Universal Service Administrative Company.

NOTE: These dollars represent submitted claims to USAC for the time period January through December 1998 only, including true-ups reported to date (April 1999). District of Columbia has reported data to USAC for the entire period in question, but has not as of yet been compensated due to the fact that eligible telecommunications carrier (ETC) status has not been granted retroactive to January 1998.

ATTACHMENT C

Universal Service Administrative Company Schedule of Rural Health Care Program  
Dollars Committed Year 1

State	Dollars Committed
Alaska .....	\$34,053.57
Alabama .....	\$9,198.81
Arkansas .....	\$9,216.67
Arizona .....	\$36,626.71
California .....	\$9,525.23
Colorado .....	\$52,057.81
Hawaii .....	\$91,612.44
Idaho .....	\$5,277.50
Illinois .....	\$13,712.28
Kansas .....	\$33,316.73
Maine .....	\$1,344.16
Michigan .....	\$12,630.84
Minnesota .....	\$28,004.39
Missouri .....	\$24,451.71
Mississippi .....	\$38,183.72
Montana .....	\$106,726.75
North Carolina .....	\$21,005.41
North Dakota .....	\$83,777.85
Nebraska .....	\$11,688.33
New Hampshire .....	\$10,443.97
New Mexico .....	\$38,614.30
Nevada .....	\$21,584.88
New York .....	\$124,386.36
Ohio .....	\$28,865.94
Oklahoma .....	\$20,537.43
Oregon .....	\$6,346.38
Tennessee .....	\$9,990.61
Texas .....	\$12,278.68
Utah .....	\$29,534.58
Virginia .....	\$28,768.26
Vermont .....	\$3,789.52
Washington .....	\$12,256.55
West Virginia .....	\$1,219.80
Wyoming .....	\$1,022.52
	<b>\$972,049.69</b>

<sup>1</sup> Includes Funding Commitment Letters expected to be mailed week of 9/27/99



## ATTACHMENT D

Universal Service Administrative Company Schedule of Schools and Libraries Program  
Dollars Committed Year 1

State	\$ Amount
AK .....	\$11,932,992.58
AL .....	\$45,769,470.99
AR .....	\$13,154,643.52
AS .....	\$3,557,348.10
AZ .....	\$35,610,282.85
CA .....	\$206,391,757.29
CO .....	\$13,945,827.03
CT .....	\$23,788,196.36
DC .....	\$4,866,571.30
DE .....	\$1,006,045.70
FL .....	\$48,003,718.99
GA .....	\$77,786,315.87
HI .....	\$4,974,590.09
IA .....	\$7,266,755.15
ID .....	\$4,542,270.99
IL .....	\$78,887,519.99
IN .....	\$18,304,745.93
KS .....	\$10,181,488.23
KY .....	\$50,167,390.09
LA .....	\$39,005,354.98
MA .....	\$29,001,101.46
MD .....	\$11,486,773.49
ME .....	\$2,923,471.63
MI .....	\$56,927,837.75
MN .....	\$24,551,883.83
MO .....	\$23,641,930.13
MS .....	\$24,691,838.83
MT .....	\$3,622,895.02
NC .....	\$25,504,323.54
ND .....	\$2,408,800.40
NE .....	\$4,865,343.20
NH .....	\$1,583,922.28
NJ .....	\$61,387,902.07
NM .....	\$18,865,472.13
NV .....	\$5,213,870.49
NY .....	\$164,546,935.89
OH .....	\$57,272,501.29
OK .....	\$32,648,986.93
OR .....	\$9,377,406.30
PA .....	\$49,659,748.96
PR .....	\$47,646,855.08
RI .....	\$6,009,681.71
SC .....	\$25,041,848.84
SD .....	\$2,799,130.09
TN .....	\$27,098,296.97
TX .....	\$128,767,624.83
UT .....	\$6,154,438.20
VA .....	\$24,997,720.78
VI .....	\$2,153,443.53
VT .....	\$2,027,333.55
WA .....	\$29,903,483.48
WI .....	\$37,455,756.57
WV .....	\$9,319,829.21
WY .....	\$1,218,192.24
Total .....	\$1,660,008,866.73

Schools and Libraries Division, USAC, March 1, 1999

Mr. TAUZIN. I understand. Thank you very much. And finally Mr. Kent Lassman, Deputy Director of Technology and Communica-

tions for the Citizens for Sound Economy. Kent, your 5 minutes are started.

#### STATEMENT OF KENT LASSMAN

Mr. LASSMAN. "For every old blackboard there are hundreds of new electronic computers." That is what Dwight Eisenhower said on January 17, 1961 in his televised farewell address. Of course this speech is more famous for Eisenhower's warning to guard against the acquisition of unwarranted influence, whether sought or unsought, by The military industrial complex. But with the spirit of President Eisenhower's remark about computers firmly in mind today, we would do well to guard against the acquisition of unwarranted influence over the technology in our lives by regulation, albeit well intended.

Mr. Chairman and members of the committee, thank you for the opportunity to share my views on the E-Rate and public mechanisms to subsidize telecommunications services. I present these views on behalf of the members of Citizens for a Sound Economy Foundation.

Mr. Chairman, the problem contemplated by H.R. 1746 is real. However, the solution presented by the proposed legislation can be improved. Too often policymakers take action on the following premise: If not for government action an essential public need will not be met. This premise doesn't apply to the infusion of technology in telecommunications into American education programs.

As Mr. Shimkus pointed out, it did not apply at the turn of the century, it did not apply in 1961, and it certainly does not apply today.

The problem with the E-Rate subsidy is that it does not address a critical and one might argue the most critical aspect of education reform. If the promise of America's future is in her children and their preparedness for the social economy and social challenges of tomorrow, then we would do well to provide the tools that they will need. Unfortunately, the E-Rate subsidizes the tools that are easy to provide, not necessarily the tools that are most needed.

As much emphasis as we place on what is new and novel we should also focus on the tried and true.

The very fundamentals of education. Can our children read? Do young people have sufficient writing and logical thinking skills? Are our schools teaching children how to learn how to learn? And most important to the discussion before us today, are the Federal subsidy for telecommunication services the best use of our resources?

I suggest to you that a computer is a poor substitute for concerned parents. A computer is a poor substitute for well trained and caring teachers. An Internet connection with high speed web access is of little good to a child who cannot read at grade level. Think about your own child. Would you provide her with a computer or an inspiring teacher? Is it more important to master today's technologies or to learn the skills that permit learning the technologies of tomorrow?

Nonetheless, today's hearing is on the E-Rate. You may know that elsewhere I have recommended the elimination of the E-Rate. However, it is altogether different to ask about how to best admin-

ister the program. My written statement offers five principles that should guide any reform.

First, the program must be constitutional. The 1996 Telecommunications Act did not give the FCC the power to establish or increase taxes. In fact, had the act attempted to delegate such a power it would have been unconstitutional.

The E-Rate should also be limited. The difference between the law and the implementation of the E-Rate is stark. For example, the law says that subsidies may be granted for, quote, an evolving level of telecommunications services that the Commission shall establish periodically. But nothing about desktop computers servers, network administration, software or teacher training.

The E-Rate should be targeted. The E-Rate should be transparent, as Mr. Markey has correctly suggested, the costs as well as the benefits of the program must be made clear to consumers. One need look no further than the FCC's so-called truth in billing proposals to see how these subsidies are hidden from consumers today by the FCC.

Finally, the E-Rate should be performance based. Funding for the subsidies should be directly linked to the performance of the E-Rate program. Constitutional, limited, targeted, transparent and performance-based. These are the watch words for reform. H.R. 1746 is a step toward a better subsidy system but it can be strengthened. For example, while the sunset provision is an asset, it can be improved by a small modification to repeal the remainder of the excise tax on telecommunication services when the trust fund expires.

I see that my time has expired and I look forward to any questions from the committee.

[The prepared statement of Kent Lassman follows:]

PREPARED STATEMENT OF KENT LASSMAN, CITIZENS FOR A SOUND ECONOMY  
FOUNDATION

*Introduction*

"For every old blackboard there are now hundreds of new electronic computers." So said President Dwight Eisenhower in his televised farewell address on January 17, 1961. Of course, this speech is more famous for Eisenhower's warning to "guard against the acquisition of unwarranted influence, whether sought or unsought, by the military-industrial complex."

His early recognition of the growing role that technology might play in education seems even more relevant 38 years later, and informs the on-going policy debate about the E-Rate. And to paraphrase President Eisenhower's earlier warning about government power, today we would do well to guard against the acquisition of unwarranted influence over the technology in our lives by misguided—albeit well intended—regulatory policy.

Mr. Chairman, and members of the Committee, thank you for the opportunity to share my views on the E-Rate and public mechanisms to subsidize telecommunications services. I present these views on behalf of Citizens for a Sound Economy (CSE) Foundation's members. At CSE Foundation, I am the deputy director for technology and communications policy.<sup>1</sup>

More than a quarter of a million strong, CSE Foundation's members are in every corner and congressional district of America. Our members distinguish themselves as policy activists. They constantly remind us that decisions made in Washington, D.C. are felt in places far away from here. And that is where CSE Foundation can be found. We fight at the grassroots level for lower taxes and less economic regulation. CSE Foundation members are also consumers. They understand from their own personal experiences how markets and competition—not government regula-

<sup>1</sup> CSE Foundation does not receive any funds from the U.S. Government.

tions—enable individuals to make better decisions about the products and services they want and need, including telecommunications services. Public policies we are here to discuss today should seek to increase, and not limit the choices, control, and information available to consumers.

The E-Rate, and the taxes collected from consumers to support it, have long been interests for CSE Foundation. At the most basic level, the E-Rate is a part of a complex wealth transfer system where the units of value are telecommunications services. The E-Rate is based upon a policy that takes from one consumer in order to give to another consumer; the effect is to distort the marketplace and to be inherently unfair.

The legislation before you today, H.R. 1746, correctly identifies a problem but presents a solution that would be—at best—a marginal improvement over the current situation. More likely, it would result in an unfunded entitlement that might actually limit opportunities for America's children to learn from, and by, using technology.

#### *The Problem*

Too often policymakers take action based on the following premise: If not for government action—a new program, a new law or subsidy—an essential public need will not be met. This premise does not apply to the infusion of technology and telecommunications into American education programs.

One week ago, on the 23rd of September, the Associated Press ran a story about a report featured in *Education Week* that detailed the prevalence of technology in American schools. All told, there are 5.7 students per instructional computer. 71 percent of our schools use the Internet in a classroom. It is simply incorrect to claim that computers and Internet access are not available to our students.

Despite its overwhelming size and the speed by which the E-Rate has grown, growth of technology in the classroom has not been the result of this federal policy. Looking forward, it is more likely that local administrators and teachers working with parents and the local community will make the decisions for what will work in their schools. This suggests that any subsidy program should have clear goals and should be phased out upon their completion.

A second problem with the E-Rate subsidy is that it does not address a critical—one might argue the most critical—aspect of education reform. If the promise of America's future is in her children and their preparedness for the social, economic, and international challenges of tomorrow, then we would do well to provide the tools that they will need. Unfortunately, the E-Rate subsidizes the tools that are easy to provide—not necessarily the tools that would most add value to our students, society, and economy.

Technology has wrought great change in America. An extensive review of these changes would not surprise or necessarily inform the members of this committee. Our jobs, workplaces, leisure, education, and social networks have responded to the advances of information technology.

However, some things do not change. As much emphasis as we place on what is new and novel, we should also focus on education fundamentals. Can all of our children read? Do young people have sufficient writing and logical thinking skills? Are our schools teaching children to learn how to learn? And most important to the discussion before us today, is a federal subsidy for telecommunications services the best use of our resources? Can a computer or an Internet connection teach a child the habits of the mind to understand basic mathematics and science? Will tomorrow's workers know how to communicate and think as a result of a new technology subsidy system today?

I suggest to you that a computer is a poor substitute for concerned parents; a computer is a poor substitute for well-trained and caring teachers; an Internet connection with high-speed web access is of little good to a child that cannot read at a basic level.

And if the recommendations that I present today are too challenging, consider the following thought experiment to help guide your decisions. Would it be better provide your own child with a mastery of today's technologies without the skills that permit learning the next set of technologies? Or, would it be better for your daughter, or your son, to have the skills to maximize her own, or his own, flexibility in the workforce and in society?

Obviously, it is the latter. Children must be taught how to think critically, to learn on their own, and to communicate with others. Technology can augment this process. It is not however, a stopgap or substitute for something else entirely, namely a basic education. The skills most attractive to employers are not centered on web-browsing. For example, computer programming requires a solid foundation in analytical skills—basic mathematics and science.

A federal subsidy program for telecommunications services is the wrong way to address fundamental education reform.

*Principles for Reform*

All of universal service, and in particular the E-Rate program, is in need of a comprehensive overhaul. Following are a handful of principles to guide any such effort.

*It should be Constitutional.* The 1996 Telecommunications Act did not give the Federal Communications Commission (FCC) the power to establish or increase taxes. In fact, had the act attempted to delegate that power, it would be clearly unconstitutional.

A power delegated in the Constitution cannot be re-delegated. This is the starting point of a legal theory called the non-delegation doctrine. The non-delegation doctrine is not a musty relic from history. On May 14, 1999 the 10th Circuit struck down air quality regulations promulgated by the Environmental Protection Agency (EPA) on the basis that the agency was implementing regulations not expressly approved by Congress. In *American Trucking Association v. United States Environmental Protection Agency*<sup>2</sup> the court held that without a clear standard from Congress, the EPA could not constitutionally create and mandate rules and regulations. This need for a clear statutory standard is consistent with Supreme Court decisions such as *Industrial Union Department v. American Petroleum Institute*<sup>3</sup> and *J.W. Hampton v. United States*.<sup>4</sup> As in these cases, there is no clear statutory standard by which the FCC can create or increase taxes to fund the E-Rate program. If Congress does not administer the E-Rate, then it is imperative that a clear statutory standard is established to provide guidance to, and legal authority for, the its implementation and administration.

While the Supreme Court has not ruled on the question of a clear statutory standard for the E-Rate, a hint of the Court's opinion might be gleaned from the opinion in *AT&T Corp. v. Iowa Utilities Board*.<sup>5</sup> Justice Scalia, writing for the majority, declared that "It would be gross understatement to say that the Telecommunications Act of 1996 is not a model of clarity. It is in many important respects a model of ambiguity or indeed even self-contradiction."

*It should be limited.* Federal support programs for telecommunications services should be consolidated and limited. The General Accounting Office has identified 40 subsidy programs to support telecommunications services. In addition, section 254(h)(B) of the 1996 Telecommunications Act requires a discount to be provided to schools, libraries and the like for the services of a telecommunications provider. The current administration of the E-Rate is not limited to telecommunications services as contemplated by the law. Finally, reform of the E-Rate should include a sunset provision for the program. Without such a measure, the E-Rate will become an entitlement that hides and distorts budget decisions in local school districts.

*It should be targeted.* A subsidy for the needy—students, rural health facilities, or local libraries—should be targeted to those in the most need. Pressure to better target the federal largesse of the E-Rate will grow as limits to the size, scope, and duration of the E-Rate are implemented.

*It should be transparent.* Section 254(b)(5) of the 1996 Telecommunications Act requires that universal service programs adhere to a principle of specific and predictable support mechanisms. Section 254 (e) of the 1996 Telecommunications Act requires all subsidies to be explicit. As a result, any reform to universal service—including the E-Rate—must rely upon a predicable source of revenue that is collected in an open manner from consumers. The current mechanisms to fund universal service do not meet this minimal standard. An improvement to this standard would be to require that in addition to making the costs associated with universal service explicit, the benefits (and beneficiaries) of universal service subsidies should also be made clear to consumers.

*It should be performance-based.* Funding for the E-Rate should be directly linked to the performance of the program. This simple guideline would create an incentive to limit wasteful spending. If students were to learn more through additional appropriations for the E-Rate, then the program would likely thrive. If, however, students did not fare better despite extravagant expenditures for E-Rate funding, then America would be best served by spending those precious dollars on a more effective education program. In addition, this principle creates a means through which the merits of the program—if they exist—will be justified by an honest taxpayer assessment.

<sup>2</sup> 1999 WL 300 618 (D.C. Cir. 1999).

<sup>3</sup> 448 U.S. 607 (1981).

<sup>4</sup> 276 U.S. 394 (1928).

<sup>5</sup> 119 S.Ct. 721 (1999).

A significant problem with funding a government program through an excise tax—either alone or funneled through a trust fund—is that it divorces the results of a program from the source of the revenue. Consider that as consumers spend more money on telecommunications services the amount of funding for the E-Rate will continue to climb regardless of need or efficacy of additional revenues.

An assessment by taxpayers—most often through the Congressional oversight process—requires objective measures of success. Currently, we measure the amount of money that goes into the E-Rate program. However, it would be more helpful to know how much of the multi-billion dollar E-Rate program makes it into the classroom versus being spent on administrative costs. Is web access as good of a teaching tool as a local area network run by teachers trained in HTML? Does this question produce different answers at different grade levels? These questions, and not numbers about the quantity of applications for federal aid, would do more to help understand the merit and performance of this federal subsidy. In turn, better information about the performance of federally funded program can translate into a better use of scarce resources.

#### *Reforming Reform: H.R. 1746*

Common wisdom suggests that unless Congress, or the FCC, steps into the marketplace with a tax and regulatory system then our schools, libraries, and rural health care providers will not have adequate telecommunications services. If that were true, and if a federal subsidy were introduced, then we would certainly attempt to design the most efficient system to administer that subsidy. H.R. 1746 is a step toward a better subsidy system that the current E-Rate program. However, this proposed legislation can be *significantly* improved.

The principles outlined above should guide any effort—including the development and refinement of H.R. 1746—to reform the E-Rate program. Following are only a few examples of where this legislation can be improved.

- People use the Internet. Students, library patrons, and rural health care professionals are not the direct beneficiaries of the E-Rate. H.R. 1746 would make resources available to states, not to schools and certainly not to students. The closer a subsidy is moved to the ultimate beneficiary, the better and more accountable the subsidy system.
- The sunset provision in H.R. 1746 is very important. It, however, could be improved by repealing the remainder of the federal excise tax on telecommunications at the same time that the proposed trust fund expires. This excise tax was introduced to fund the Spanish-American War. The war lasted approximately three months and ended more than 100 years ago. It is time to get rid of this tax.
- By definition, a program funded by an excise tax is poorly structured. The excise tax—a tax on talking—should be repealed and the E-Rate should be funded out of general revenues. This structural change to H.R. 1746 would strengthen the proposal to reform the E-Rate.
- A criterion such as “living in a sparsely populated area” is not the same as an area in need of a subsidy. For example, some rural areas may be served by wireless telecommunications services at a lower cost—and therefore lower need for subsidy—than traditional landline services. A change of perspective from rural to high-cost would better target the resources made available by the E-Rate program.
- H.R. 1746 sends unexpended balances in the trust fund to the general treasury. At the same time, consumers are led to believe that the telecommunications taxes that they pay are putting computers in a classroom. Taking money for one purpose, putting it in a trust fund, and then spending it on another purpose is not good public policy. It is dishonest. Instead, any subsidy program should be funded out of general revenues, where it would have to compete with other priorities. If this change is not made, at the very least, unexpected balances should be returned to taxpayers, and not shifted into an already-bloated federal budget.

#### *Conclusion*

This impetus behind H.R. 1746 is well-intentioned. The current E-Rate is a case study in government waste, fraud, and abuse. However, the proposed reforms contained in this legislation should not go forward without substantial improvement based on the principles outlined above.

As we move forward, I trust that we will heed the warning of President Eisenhower to “guard against the acquisition of unwarranted influence, whether sought or unsought.”

Thank you.

Mr. TAUZIN. Thank you very much. The Chair recognizes himself quickly. The GAO study that looked at the beginnings of this program was highly critical of it and criticized the corporations that were created to carry the program out, even indicated to all of us that there were 27 existing programs that could provide funding for the purchase of technology for schools and libraries and questioned the need for corporations that were not subject to ordinary congressional oversight review and appropriation.

What became of that study and what was done? Perhaps Mr. Wright you want to get into that? What was done to respond to that GAO study?

Ms. PARRINO. There were a number of GAO studies. GAO came in to look at our operating procedures. They made a number of recommendations for improvement. As an example, they suggested or highly recommended that our internal auditors complete—or that our independent auditors completely review before we issue any commitments to schools and libraries. And we adopted that recommendation and implemented it so we completed our audit—

Mr. TAUZIN. They called these corporations illegal at one point, didn't they?

Ms. PARRINO. In a response, I believe to Senator Stevens and Senator McCain, they identified or raised concerns and issues. As of this point in time, both of those corporations have been merged into USAC and I am not aware that that opinion addressed the legality of USAC. But I would defer to Mr. Wright.

Mr. TAUZIN. So we can understand it, USAC is a corporation organized under what law?

Ms. PARRINO. USAC is a not-for-profit corporation organized and incorporated in the State of Delaware.

Mr. TAUZIN. And who created it?

Ms. PARRINO. The National Exchange Carriers Association suggested to the Commission that they should create an independent entity that was neutral primarily for—at that point in time for the administration of the High Cost Fund.

Mr. TAUZIN. So the Commission asked for its creation or created it?

Ms. PARRINO. The National Exchange Carriers Association suggested or recommended to the Commission that they—that NECA create an independent corporation.

Mr. TAUZIN. So the association created this corporation?

Ms. PARRINO. That is correct.

Mr. TAUZIN. And this corporation now administers these funds. Who collects these funds? Where do they come and where do they go?

Ms. PARRINO. The Universal Service Administrative Company collects the funds, the FCC establishes the rate on a quarterly basis and based on that order we collect the funds that the FCC designates.

Mr. TAUZIN. An agency of government decides how much telephone users are going to pay, and then instructs a private corporation organized under the State of Delaware to collect the money and distribute it? Is that an accurate description? Mr. Wright?

Ms. PARRINO. I will defer to Mr. Wright.

Mr. TAUZIN. I want to know how the legal is set up. We have another corporation called ICANN we have been looking at in the Internet services area, a private corporation, and the way these private corporations function in connection with associations and government agencies always intrigues me. In this case, you decide how much is going to be collected from each telephone user's bill; is that correct, Mr. Wright?

Mr. WRIGHT. No, Mr. Chairman.

Mr. TAUZIN. How do you do that, then?

Mr. WRIGHT. The money is collected from telephone companies, not from users.

Mr. TAUZIN. Telephone companies collect it from their users.

Mr. WRIGHT. They can.

Mr. TAUZIN. Where do they get it? Out of the sky?

Mr. WRIGHT. They have three choices. Like anybody else when they have a fee imposed on them, they can pass it on to their users.

Mr. TAUZIN. Or they could assess their stockholders.

Mr. WRIGHT. Lower their profits or decrease their rates.

Mr. TAUZIN. Wait, wait, stop, they can't take it out of profits without taking the same money out of their consumer. The money comes from consumers, doesn't it? Let's not beat around the bush.

Mr. WRIGHT. Absolutely.

Mr. TAUZIN. So the dollars you assess the corporation are going to be assessed to their consumers, us, telephone consumers.

Mr. WRIGHT. That is what usually happens.

Mr. TAUZIN. So without playing games, when you tell a corporation you want so much money from it you are telling it to go out and collect it from its consumers and obviously it is going to show up on my bill and your bill.

Mr. WRIGHT. We are certainly aware that that has happened. We have been deregulatory in our approach.

Mr. TAUZIN. Do you think it is a mystery that it happens?

Mr. WRIGHT. No, Mr. Chairman.

Mr. TAUZIN. Normally, when taxes or fees are assessed against corporations, don't they pass those on to their consumers as part of the cost of business? That is normal, so you know in advance when you assess a charge against the corporation for these universal service functions that they are going to pass them on to consumers and they will show up on our phone bills; right?

Mr. WRIGHT. Most likely.

Mr. TAUZIN. So you assess these charges against them. Companies pay the money in. Where do they pay it in?

Mr. WRIGHT. To USAC.

Mr. TAUZIN. So it never goes to the Treasury?

Mr. WRIGHT. No, Mr. Chairman.

Mr. TAUZIN. The United States Treasury never sees this money?

Mr. WRIGHT. That is right.

Mr. TAUZIN. The money goes to a private corporation set up under the laws of the State of Delaware. What relationship do you have with this private corporation?

Mr. WRIGHT. They are our agent, Mr. Chairman. As Ms. Parrino said, they are the successor to NECA, which has been in existence for years and was largely praised as an example of outsourcing by us, rather than doing it in-house.



Mr. TAUZIN. I am not heaping scorn or praise. I am just trying to understand. So this corporation is your agent? It is an agent of a government agency.

Mr. WRIGHT. For decades in the high cost area NECA and now USAC have collected money from telephone companies to support the High Cost Fund.

Mr. TAUZIN. And now this corporation acting as your agent disburses money. Does any committee of Congress, the appropriators who oversee the collection and expenditure of Federal dollars ever audit, account for, appropriate and oversight collection and spending of this money?

Mr. WRIGHT. Well, this Congress of course enacted section 254(d), which requires us to assess telephone companies.

Mr. TAUZIN. Does any appropriator oversee the collection and expenditure of this money? Do you go to any Appropriations Committee with this business?

Mr. WRIGHT. I don't know the answer to that.

Mr. TAUZIN. Ms. Parrino, do you? Do you appear before an Appropriations Committee to talk about how this money is collected and spent?

Ms. PARRINO. No, I do not. I administer the rules and the orders as directed by the Federal Communications Commission.

Mr. TAUZIN. So you just follow their direction, but nobody in Congress ever oversees the collection and expenditure of that money?

Ms. PARRINO. We do not appear before the Appropriations Committee. But USAC has been subject to audits from the General Accounting Office.

Mr. TAUZIN. Is the money that is collected out of this system part of the budget of the United States, Mr. Wright?

Mr. WRIGHT. I don't believe—it doesn't go into the Federal Treasury. I am not sure what the question is. I do know there has been no shortage of oversight of the Schools and Libraries Program. Congress can't be faulted for that.

Mr. TAUZIN. You are saying, though, that it never goes to the Treasury? It is not counted in the budget?

Mr. WRIGHT. I know that—

Mr. TAUZIN. If it disappeared tomorrow, would there be an offset required under our budget laws? Do you know?

Mr. WRIGHT. I don't know the answer.

Mr. TAUZIN. Mr. Lassman, do you know the answer?

Mr. LASSMAN. Mr. Tausin, it is on the budget. It has been since 1997.

Mr. TAUZIN. So it never goes to the Treasury but it is in our budget and the appropriators never appropriate it or manage it in any respect? Do I have it accurate now? In that regard, Ms. Parrino, who is on this—who serves on this corporation? Who selects the members of it? Where do they come from?

Ms. PARRINO. You are referring to the board of directors, Mr. Chairman?

Mr. TAUZIN. Whoever runs the corporation. Is it run by a board?

Ms. PARRINO. There is a board of directors of the corporation. The board represents various constituencies that either benefit or pay into the various programs. It is a 19-member board. The industry representation is spelled out in an FCC order.

Mr. TAUZIN. So it is all done by FCC order. Do you make decisions about who gets money or does the FCC tell you who should get money?

Ms. PARRINO. We make the decisions on who gets money on each of those programs consistent with FCC rules.

Mr. TAUZIN. They make general rules and then you make specific allocations?

Ms. PARRINO. That is accurate.

Mr. TAUZIN. One final thing. I was looking at one of your programs, the Health Care Program, where you administered almost \$1 billion of money. There are lots of States that didn't get any money. Why is that?

Ms. PARRINO. Which program is that?

Mr. TAUZIN. Your Rural Health Care Program. I am looking for my own State. My own State, I don't even see it on the list. Some States were just left out.

Ms. PARRINO. It depends upon the rates that are established in your State. To the extent that your urban rates are very comparable to your rural sites, again to the extent the High Cost Program provides significant subsidies in Louisiana, there would be no subsidy in rural health because that particular program says to the extent rural rates are higher than urban rates—

Mr. TAUZIN. I think it would be very good if we got just a one-page explanation of the rules by which all of these moneys are distributed.

Ms. PARRINO. I would be happy to do that.

[The following was received for the record:]

The Rural Health Care Division (RHCD) of the Universal Service Administrative Company (USAC) administers the support program that was authorized by Congress and designed by the Federal Communications Commission (FCC) to make telecommunications services—including the more “cutting-edge” services—affordable for rural health care providers (RHCPs). Discounts apply to monthly telecommunications service charges and installation charges, but not to terminal equipment costs.

What this means to RHCPs is that support is available for any telecommunications service, including T-1, fractional T-1, and ISDN. Support is also available for limited long distance charges to an Internet Service Provider (ISP). Level of support is determined by the location of the RHCP and the type of service chosen by the recipient. This will be calculated individually for each RHCP. Additionally, if an RHCP is already receiving services, they can opt to save on that service, or upgrade to another. Prior to committing to anything, RHCPs have an opportunity to know their level of support.

In order to receive a discount, the primary concern for the RHCP is to make sure that they are eligible. They should be a rural health care provider, or, regardless of location, have no other means of reaching an ISP than by making a long distance phone call. They must also be a public, not-for-profit entity.

After determining eligibility, it is important for RHCPs to have a clear understanding of how they will use the telecommunications services. For example, will they need to download information from the Internet? Will they need to transmit data, images, or interactive video? How fast will they need to send or receive data? With whom do they plan to communicate most? At this point the eligible RHCP identifies their telecommunications needs and submits Form 465 to the RHCD. The RHCD will then post Form 465 on their web site for 28 days so that telecommunications companies can contact them with service offerings. RHCPs may also approach service providers directly to encourage bids. The RHCP then chooses the service provider and the services they want, and notifies the RHCD by submitting Form 466, in addition to Form 468 which is completed by the service provider and is used by the RHCD to verify the services and calculate the discounted rate. Once the RHCP begins receiving services, they notify the RHCD by submitting Form 467. The RHCP is then billed by the service provider at the discounted rate. The service provider recovers the difference from the Universal Service Fund (administered by

the RHCD). This process must be completed annually in order for RHCPs to continue to receive discounts on services.

Mr. TAUZIN. Apparently there are some formulas that might be very interesting to members if you kindly submit that to the record.

The Chair is pleased to recognize the gentleman from Illinois, Mr. Rush.

Mr. RUSH. Thank you, Mr. Chairman. Let me go back to Ms. Parrino. Ms. Levy of the NTIA testified earlier that a large startup cost would be required if the program were moved to that agency. She indicated about—she testified about the large startup costs. Do you know how much you save if the E-Rate program went to the NTIA given that your organization would continue to be required to administer various other universal service programs such as the high cost and low-income subsidy programs?

Ms. PARRINO. If the NTIA were responsible for the Schools and Libraries Corporation Program, USAC would no longer incur any expenses associated with that program. We do have separate budgets for each of the other three programs which would still be in place. The Schools and Libraries Program is the largest chunk of the USAC consolidated budget. I don't have a percentage for you. I do have specific dollars that would be left or costs that would be left to administer the other programs. I don't have a percentage for you. I could certainly provide that.

Mr. RUSH. Would you, please?

Ms. PARRINO. Yes.

Mr. RUSH. Wouldn't this bill that we are currently considering, wouldn't that result in increased administrative costs for your agency?

Ms. PARRINO. For USAC?

Mr. RUSH. Yes.

Ms. PARRINO. I don't know what the overall impact would be. Again as far as my expenses and my budget, my budget would decrease because I would no longer have responsibility for that function.

Mr. RUSH. Maybe I should ask that question to Ms. Levy. Would there be an increased cost to your agency if, in fact, this bill were to pass?

Ms. LEVY. There would be. We don't have—we have other grant programs in place at NTIA but they are set up to function differently than a program like this, which is more of a block grant program. So we would have both staff and infrastructure costs.

Mr. RUSH. Staff and infrastructure. So there would be an increase?

Ms. LEVY. There would be.

Mr. RUSH. Okay. And would that be taking money away from the students that we are trying to service if, in fact, you had additional costs at your agency?

Ms. LEVY. It would take away money from the overall fund.

Mr. RUSH. Mr. Wright, it seems that the people actually affected by the Schools and Library Program, there are not many complaints from those individuals, the beneficiaries of the programs and even the companies. Do you agree with that?

Mr. WRIGHT. As I understand it, they are quite pleased with the way the program is going and hope it will continue.

Mr. RUSH. You testified earlier about court decisions and the Fifth Circuit decision that put to rest the legal challenge that universal service is a tax. Don't you think it is kind of inconsistent and disingenuous—you might not want to answer it in the way that I ask, but please—for the Congress to be pursuing and continue to be recalcitrant in its position that this is a tax when the Court of Appeals, the Fifth Circuit, has actually made a decision saying that it is not a tax?

Mr. WRIGHT. Let me say this. I had the pleasure of testifying before the House Ways and Means Committee last year on this, and I said that, gee, if we lost in the Fifth Circuit this would be a good fallback. But indeed we won in the Fifth Circuit and perhaps I can tie it to your earlier question to me that the Schools and Libraries filed a very nice amicus brief on our behalf in the Fifth Circuit defending our position in toto and that was helpful.

Mr. RUSH. And are you aware of an earlier decision yesterday by Senator McCain that he strongly endorsed the E-Rate funding?

Mr. WRIGHT. I did read about that in Communications Daily yesterday. And, you know, just for the record this has always been a bipartisan program. Senators Snowe and Rockefeller also filed an amicus brief in the Fifth Circuit fully supporting how the FCC had implemented the program.

Mr. RUSH. I want to return to Ms. LEVY. What types of services does the E-Rate program support that would not be supported by H.R. 1746? And then conversely, what type of services not currently supported would be included under H.R. 1746? And the third part of that question is wouldn't they be basically the same type of programs?

Ms. LEVY. Yes, as I read the proposed legislation, I think the program itself would be very similar. I think Mr. Wright has identified some areas where the legislation is ambiguous and it might go to litigation on that. I think the major difference is in the administration of the program. It would be taken away from the FCC and it would be given to NTIA to run as more of a block grant program that received an appropriation.

Mr. TAUZIN. The gentleman's time has expired. Let me try to get one more round of questions before we have to break. Mr. Cox.

Mr. COX. Mr. Wright, I am wondering if you didn't just misspeak in response to Mr. Rush when you said we won it on the taxing issue in the Fifth Circuit. You didn't really win the question of whether that was an unconstitutional tax.

Mr. WRIGHT. The origination clause issue was the primary issue raised by Celpage that said it was an unconstitutional tax under the origination clause.

Mr. COX. Oh, the origination clause is the issue of whether the bill starts in the House or the Senate. The unconstitutionality of the tax, that is whether you can levy it or Congress can. You didn't win that issue, did you?

Mr. WRIGHT. That was the taxing clause issue.

Mr. COX. And you didn't win that, did you?

Mr. WRIGHT. There was a footnote that says we win it on two grounds. First, that they did not raise it and, second, that there is no merit to it anyway.

Mr. COX. Well, actually, I have the footnote and it is right in the text, and I have it before me. It says that Celpage raised it in their reply brief, therefore, we will not consider it. And I mean if a Court doesn't consider the question, then it doesn't decide it in your favor. Isn't that right?

Mr. WRIGHT. In footnote 52 the Court went on to say even if Celpage's taxing clause issue were properly before us we find no basis for reversal and went on in a few sentences to explain why there was not merit to it.

Mr. COX. The Court said it didn't consider the issue, right?

Mr. WRIGHT. And alternatively said in any event there is no merit to it.

Mr. COX. Did the Court consider and decide the question?

Mr. WRIGHT. I would certainly say that the issue has been waived at least. And the Court has said there is no merit to it.

Mr. COX. Actually, I disagree strongly with your interpretation of the opinion because it says in plain English: Therefore, we will not consider it. The Fifth Circuit did not consider your issue. That issue. It didn't decide it in your favor. It is not a decided issue. It is not stare decisis. It is not binding on anybody. It is not the law of the land in the Fifth Circuit or anything else.

Mr. Lassman, did you want to say something on this?

Mr. TAUZIN. I think we have a minute left. We have a vote on.

Mr. COX. I can resume questioning when we get back.

Mr. TAUZIN. Why don't we do that. We will resume questioning when we get back.

[Brief recess.]

Mr. TAUZIN. Thank you for your patience, ladies and gentlemen. Several of the members are coming, and I am going to have to leave you to attend a technology summit right now. But Chris Cox from California will assume the Chair and continue his round of questions and recognize members in order. And again I appreciate your consideration for interruptions like this.

Mr. Chris Cox from California.

Mr. COX [presiding]. Thank you, and if the interruption on the floor results in our members not returning, then what I would like to do is ask all the members of the panel if they would be willing, and it may be an easy promise to make, to respond to additional questions in writing that we would submit that members might have.

Ms. Levy, the FCC has recently increased the amount of the E-Rate tax. It was on an annual basis a billion, and now it has been increased to \$2.25 billion.

Ms. LEVY. I think it went from \$1.3 to \$2.25.

Mr. COX. And so right now there is an exaction without prejudicing the argument about whether and how this acts as a tax. There is an exaction from the economy, to put it broadly, because we had this exchange with Chairman Tauzin about how it functions and what the FCC expects will happen when it makes these actions, but we do have an exaction of \$2.25 billion that we

are now going to levy on the economy, the U.S. economy. Is that essentially the case?

Ms. LEVY. Well, I believe that 2.25 is the full funding of the program as originally envisioned by both Congress and the FCC. It was brought down because of problems they were having during the first year.

We would respectfully disagree with calling it a tax.

Mr. COX. That is why I said it is an exaction. To use really simple Anglo-Saxon words, we are going to get \$2.25 billion out of the economy under the aegis of this exaction. Is that not the case?

Ms. LEVY. And we will put it back into the economy.

Mr. COX. I understand.

Ms. LEVY. I think that is right. We are asking for \$2.25 billion from companies that are participating in the program, which I think it is consistent with how the statutory language was put in in terms of talking about this as part of the universal service fund, talking about this as an evolving definition of universal service.

Mr. COX. There is a levy of \$2.25 billion and just to do some big number math off the cuff here—we won't need a calculator, we will do it rough justice—but if there is about a quarter of a billion people in America, and you have got \$2.25 billion then something just shy of \$10 a head is this exaction for every man, woman, child and infant in America. Is that not right?

Ms. LEVY. I don't think it is that much. I think if you see what people are paying on their phone bill.

Mr. COX. No, no, I think it is that much because it is pretty simple math. I will ask the question differently. If you divide the exaction, which is \$2.25 billion, by a quarter billion, what is the answer?

Ms. LEVY. I agree with where you are going.

Mr. COX. There you go. We are talking about \$9 and change, round figures, \$10 per head. So in my household where I have three little kids, it is exaction on our family, unless we have some way to get through a loophole that most Americans don't have, net on average, the exaction on our family is \$50 from this exaction which we won't call a tax. We are taking it away. My point is these are big numbers. And this is a program that Congress has not expressly authorized. The Congress has had nothing to do with these figures. Congress didn't come up with the \$50 per household number for my household. Congress didn't come up with the \$10 per capita amount of the tax. You guys came up with that.

Ms. LEVY. The FCC came up with that.

Mr. COX. Right. Do you understand why Democrats and Republicans in the Senate and in the House have written these letters saying that we don't have King George any more and Congress has this authority and the executive branch doesn't? That is a big amount of money to do in the executive branch without Congress being involved in any way. Don't you think?

Ms. LEVY. I understand. Yes, if it is a taxation issue, then it is for Congress to decide.

Mr. COX. Even if one were willing to hang his or her hat on some seemingly comforting language in a footnote that didn't decide the question, as a matter of policy do you think that billions of dollars ought to be taken away from the economy and then put back in in

more pleasing ways without Congress as a policy matter being directly involved in that process on a regular basis?

Ms. LEVY. I think that when we are talking about taxation issues, it is up for Congress to decide. I think Congress did make a commitment and did make a conscious move in the 1996 Telecom Act to establish a universal service fund that had a schools and libraries component that would do what the program is doing. And that is provide E-Rate moneys to children in schools and libraries throughout the country. I think the FCC has simply implemented what it has deemed to be the congressional mandate of the Telecom Act.

Mr. COX. Mr. Lassman, you have been trying to interject.

Mr. LASSMAN. If I could make a clarification of what is being discussed, Congress very clearly, and the President signed a bill that told the Commission how to exact that amount of resources, the amount of resource being defined as an evolving series of definitions. They didn't say to what extent, they did not say a number, they didn't say so much per year. And that difference, that clarification of delegation is very important because the Supreme Court has ruled extensively over the last 100 years that "to what extent" is a standard that must be met. The Congress has to tell a regulatory agency to what extent may you regulate.

Mr. COX. We have got 37—by the estimate provided to members here on the committee, we have got 37 State and local exactions, taxes, I think we can say State and local taxes on telecommunications in the United States. This morning I just had a news conference with Senator Wyden in the Senate radio and TV gallery unveiling legislation that I think we are going to work with Larry Summers on that puts U.S. policy on the side of a global permanent moratorium on Internet taxes and tariffs around the world. We have got the WTO meeting coming up in Seattle in November, and we believe that it is in America's best interest to take the temporary moratorium that we have and make it permanent around the world. We want a 1-year standoff at that WTO meeting.

And the reason that we are concerned about it is that France, for example, has a 20.6 percent value added tax. And if France decides that it wants to apply its VAT as the EC recommended in 1998, not only to goods traded over the Internet but also the information, to software, service going over the Internet, and that is just one country, you can very quickly see how these exactions accumulate and end up killing the goose that is laying the golden eggs, which is in this case the Internet and the possibility that it holds.

In the U.S. we have got 37 different taxes and we have also got some 30,000 jurisdictions that could, if they chose to do so, levy taxes.

My question to anybody that wishes to address it is whether or not, as reasonable as it might be for each one of these tax jurisdictions, and the FCC for its part to say, we are only going to take our little corner here, ought we not be concerned about the aggregation of all these charges inasmuch as the Internet is a global medium and might we not by our bad example defeat what we are trying to accomplish at the WTO and elsewhere if we are adding

new taxes even though they are not authorized by Congress onto telecommunications?

And last, inasmuch as telecommunications itself is an elusive thing that we are increasingly having difficulty defining, should we be a little bit wary about taking existing concepts, for example, of universal service, which we have always felt comfortable applying to a telephone system to subsidize local users with long lines, for example, and applying it to whatever in the world telecommunications might become because telecommunications might become something very different and we might have trouble recognizing it in the future.

What we did in the Internet Tax Freedom Act of course is put a ban on taxes for Internet access. Any kind of telecommunications service that includes Internet access already runs smack in the middle of the Internet Tax Freedom Act. And so I just wondered whether or not this approach doesn't make more sense inasmuch as it gets you into general appropriations for block grants for ultimately the purpose that we are seeking to achieve here, which is schools and libraries, without using an interfering mechanism of taxing telecommunications and being the "Nth" tax on top of all of these other exactions.

Does anybody want to deal with that?

Mr. WRIGHT. If I could respond, I am sure there is no dispute from anyone, and certainly not from the FCC, that Congress could always specify the amounts in these bills. And that is one of the few things that I don't think could even lead to further litigation.

If I could just explain our perspective for a minute—

Mr. COX. I will just interject on that point. If the executive levies a tax on the country and the Congress by bicameral action passes a bill repealing that unconstitutional tax, and the President vetoes it, then you are still left with the problem, aren't you?

Mr. WRIGHT. I was suggesting that if Congress passed a law saying X dollars shall be—

Mr. COX. As long as the President went along with it. As long as it is the same executive branch that came up with this program against Congress' wishes went along with it, it is fine. But I am not sure for Congress to have to reassert itself and then to depend on the executive's approval is the right policy question.

Mr. WRIGHT. Imagine our perspective on the high cost issue. There is no question—I am sure no one would disagree that we have been instructed in section 254 to subsidize rural residential customers, as Mr. Markey was noting before. The Act does not tell us how much we are supposed to raise for that purpose either, but no one has ever suggested that we would be other than derelict in our duties if we didn't have a High Cost Fund. And, of course, Congress has to work with the President to come up with an amount, but, of course, that could be done.

But from our perspective we would be derelict in our duties if we didn't do what Congress has told us, which is establish mechanisms to support high cost and education and we have to do that. Of course, if Congress tells us how much, that make its easier for us, but we cannot not do it because the amount hasn't been specified.



Mr. COX. Do you want to take a stab at whether we are better off with the Tauzin approach, which does not add an incremental exaction on telecommunications?

Mr. WRIGHT. Well, my thought on that was that it would probably lead to another round of litigation. The bill seems to me to say that it is supposed to fund internal connections and Internet access, but it doesn't say that in so many words. And I can imagine some Telco saying, going to court and saying, well, Congress meant to fund something different and that is why they passed a new law. And, therefore, the law also directs the Department of Commerce to conduct a rulemaking to determine what is to be funded, so they would have to do that. And the litigation would follow, and the arguments would be made, well, Congress meant something different or they would not have passed a new law.

On the other hand, if Congress means to do just the same thing, the aspect of Congressman Tauzin's bill that specifies the amount, you know, we, of course, in the FCC and I am sure at NTIA will do whatever Congress tells us to do. And that specifying the amount just make its easier.

Mr. COX. And I am not sure I understand whether you are taking a position on whether we would be better off to use general appropriations rather than a specific levy on telecommunications?

Mr. WRIGHT. I don't think the FCC has a position on that. Our position is that we administer the Telecommunications Act.

Mr. COX. From a policy standpoint, as I say, a lot of us are very, very concerned about the multiplicity of different kinds of taxes and so on.

Well, I think I have extended my own time for questioning under our rules substantially but I did so for the purpose of seeing whether other members would arrive, and they have begun to arrive, and so I would recognize the gentlewoman from New Mexico if she wishes to be recognized.

Mrs. WILSON. I may not help you out, Mr. Chairman. I am beginning to understand some of the intricacies of this. I was not here, as you know, when the 1996 Telecom Act was passed. Although I have seen what it does in my local community, which is to provide access to the Internet, particularly for elementary, middle and high schools who did not have that access.

And unlike Mr. Markey, New Mexico is a rural State and I do believe that universal service is a laudable goal, just as the electrification of America was a laudable goal in the 30's and 40's. The people who live in rural areas shouldn't be left out. I happen to believe that it is probably more important for our elementary schools to have great teachers and good books and fine curricula than it is for them to have computer labs and access to the Internet. But I am also forward-looking enough to know that that may not be the case 10 or 20 years from now, and that all children should have access to the information that increasingly will be available on the World Wide Web when it is not available in their local library.

As to the constitutional issues and how we decide who has the power to tax and whether the 1996 Communication Act gives the FCC the authorities that it has taken and how so if they are limited, that is not my area of expertise. I am not a lawyer, thank goodness, and I look at this with a fairly practical eye of what is

its effect? Is it being administered properly? What would the change be for the constituents that I represent if we change the way this is being administered? And for that reason I am fairly pragmatic about all of this.

I don't have specific questions for members of the panel, and I apologize for being kind of double scheduled and not being here for your actual presentations, but I appreciate the opportunity to read through your testimony.

Mr. COX. Well, I thank you. I think as is our custom we will leave the record open for 30 days and if any member, either present or not here, wishes to submit questions I think our panel would probably be willing to respond to those questions in writing.

I won't make you swear to that under oath, but I am sure we can call you back if need be.

I appreciate very much your spending time with us this morning and your testimony has been very, very enlightening and we look forward to continue working with you on solving these problems. Thanks again.

The hearing is adjourned.

[Whereupon, at 12:47 p.m., the subcommittee was adjourned.]